

R E P O R T
OF THE
S T U D Y T E A M
O N
F i n a n c i a l A d m i n i s t r a t i o n



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MAY, 1967

ADMINISTRATIVE REFORMS COMMISSION

STUDY TEAM ON FINANCIAL ADMINISTRATION

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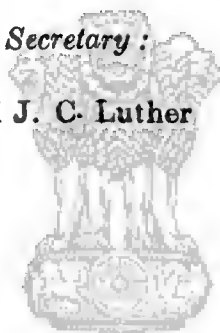
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B. Venkatappiah,
Chairman,
Study Team on
Financial Administration.

Administrative Reforms
Commission, Sardar Patel
Bhavan, Parliament Street,
New Delhi.

May 27, 1967.

Dear Shri Hanumanthaiya,

I have pleasure in forwarding herewith
the Report of the Study Team on Financial
Administration.

Yours sincerely,

(B. Venkatappiah)

Shri K. Hanumanthaiya,
Chairman,
Administrative Reforms Commission,
New Delhi.



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I N T R O D U C T O R Y
S E C T I O N



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CHAPTER I

INTRODUCTION

1.1 Our Study Team has been assigned the following subjects:

- (i) Budgetary reform;
- (ii) The system of expenditure control, including procedures for sanctioning schemes and the problem of financial delegation and decentralisation; and
- (iii) Procedures governing financial relations between the Centre and the States.

The composition of the Team is as follows:

1. Shri B. Venkatappiah	Chairman
2. Shri N.N. Wanchoo	Member
3. Shri P.L. Tandon	Member
4. Shri G.L. Bansal	Member
5. Shri N.S. Pandey	Member
6. Dr. D.T. Lakdawala	Member

Shri J.C. Luther was appointed Secretary of the Study Team.

The relevant orders are reproduced in Appendix I.

1.2 In regard to the subjects allocated, the Study Team has been asked to "ascertain facts, locate the principal problem areas, examine solutions for the problems and suggest such of them as they would recommend for the Commission's consideration." Accordingly, as one of our very first tasks, we attempted to set down explicitly and in some detail what appeared to us to be the more important issues connected with each of the three subjects of enquiry. On the basis

of this Memorandum (Appendix II), which both demarcated and mapped out the scope of our further investigations, we -

- (a) invited the views of knowledgeable persons, official and non-official;
- (b) held personal discussions with senior officers, Central and State (details of meetings in Appendix III);
- (c) initiated the collection of material and preparation of papers, on listed issues by the secretariat of the Study Team; and
- (d) organised Working Groups for more intensive study of specific aspects of the enquiry.

It follows that, for the assistance they have rendered, we are indebted to several institutions and a considerable body of individuals. To such of them as it is practicable to mention by name, we acknowledge our thanks in the concluding portion (Chapter XIX) of this volume.

1.3 Meanwhile, it is necessary to say a word about the Working Groups to whom we are specially beholden because of the valuable material they have given us on the subjects of (i) Performance Budgeting and (ii) Centre-State Financial Relations. It will be seen from the relevant Chapters of our own Report that we have drawn heavily, both in substance and presentation, from the reports of the two Working Groups. In addition, we would make appreciative mention of the study paper (on the application of the principles of Performance

Budgeting to a concrete instance) prepared by a research team of the Indian Institute of Management, Ahmedabad. The terms of reference and the composition of the Working Groups are set out in Appendix IV. The reports of the Working Groups as also of the team of the Ahmedabad Institute are set out in Volume II as accompaniments to this Report.

1.4 Volume I has 20 Chapters in all, divided into:- Introduction (Chapter I), Part One (Budgetary Reforms : Chapters II to X), Part Two (Expenditure Control: Chapters XI to XIII), Part Three (Centre-State Financial Relations: Chapters XIV to XVIII); Acknowledgements (Chapter XIX) and Summary of Observations and Recommendations (Chapter XX).

1.5 In one phrase, the theme of our Study is financial administration. Since financial administration is only part of the total process of administration, it is governed by the same principal objectives, needs, and requirements as the system of administration as a whole. It is not our province, in the present study, to spell out these factors at any length; we are nevertheless concerned with them for the purpose of locating the "problem areas" of financial administration. In spite of a changing political context, two of the basic requirements continue to be efficiency and economy within a framework of planned development, parliamentary control and federal inter-relationship. But efficiency and economy are themselves aspects of action or performance; and if there is one an-

requirement today which is more important than any other it is that policies, programmes, and administration should all be oriented to performance. These are the main elements; and, singly or together, they enter into our discussion of each individual topic in Parts One, Two and Three.

1.6 In Part One, we take up such problems of budgetary preparation, discussion, approval and execution as have an important bearing on administrative efficiency and economy on the one hand and, on the other, on the implementation of the programmes and policies of planned development. In so far as the present budgetary practices - including post-budget communication - delay action and therefore detract from efficiency, we attempt to analyse the causes and suggest remedies (Chapters VIII and IX). The same consideration, along with other relevant factors, is present in our mind in examining the suitability or otherwise of the present financial year (Chapter IV). The other Chapters in this part of the Report are concerned with rendering the budget more informative, more integrated with the processes of planning and of economic policies and, above all, a more efficient instrument of action and guardian of performance.

1.7 In Part Two, we deal with expenditure control - again in the light of the twin criteria of efficiency and economy - as only part, though an important part, of the total operational responsibility of the Government and the Parliament. The responsibility extends to the whole sphere of administration including planned development.

Since that economy is costly which consists in doing nothing, our suggestions concerning control - whether by the Parliament or by the Finance Ministry - aim at preserving initiative and delegating real authority. Parliamentary control, as we envisage it for the future, would be related to a budget of action no less than to a budget of expenditure; and this consideration underlies the broad suggestions we have made not only in Part Two (Control by Parliament: Chapter XIII) but also in Part One (Performance Budgeting: Chapter III). We deal incidentally in this part of the Report, with public undertakings; but we refrain from doing so at any length since another Study Team is in charge of that subject.

1.8 Our pre-occupation in Part III is with the need to re-adjust and re-model financial procedures, institutions and concepts in line with the changing requirements of the federal inter-relationship of the Centre and States. Our view that a somewhat radical modification is needed is based, not so much on recent political developments, as on what we believe to be the lessons to be drawn from past experience. In particular, we have in mind the actual operation of the system of financial assistance and allocation to States for implementing their Plans. We have also in mind those factors of economic change and instability which have shaken the belief that a Five Year Plan is immutable for five years. Certain other important considerations arise in the light

of the criteria we have mentioned. Not only are economy and efficiency all the more necessary in the context of planned implementation; together, these two factors make it essential that projects which involve large developmental investment should be completed without undue delay and extravagance and, above all, in practice yield the financial return on the expectation of which they have been formulated and sanctioned. If institutional measures are necessary for this purpose, they should be devised and adopted.

Financial and other supervision is essential for projects such as those we have cited, as also for the country-wide implementation of the schemes of basic importance such as family planning. With regard to schemes of other categories, however, the position is in our view different. It would be both efficient and economical - besides being desirable for other reasons - to treat the State plans as the province of the State Governments, formulated in the light of agreed priorities but otherwise untied to any condition, so long as expenditure is within the limits of allocation. This also implies that some degree of certainty as to quantum and duration would have to be introduced into the process of allocation. Another implication of the consideration which we have urged is that the Plans themselves, whether at the Centre or in the States, would have to be based on a realistic estimate of resources. It is on these and similar premises that we have based the recommendations contained in Part Three of the Report. Our suggestions include the

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PART
ONE

BUDGETARY REFORMS



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CHAPTER II

OBJECTIVES OF A BUDGET

2.1 It has been said, "Whatever else a Government may or may not do, one thing it cannot avoid doing each year if it is to continue to exist: and that is to obtain the authority of Parliament to raise revenue to meet expenditure: which is done by the Budget and the accompanying Finance Bill."*

2.2 The budget of a government is its financial blueprint for a specified period, normally twelve months. It is one of the chief instruments of financial control as well as the authorisation whereby the administration is enabled to carry out its policies and programmes. We summarise below some of the main objectives of the budgets of modern governments. In doing so we do not, of course, imply that all the aspects thus brought out should be incorporated or given equal emphasis in the Indian Budget.

2.3 (i) Accountability - This has been the outstanding feature of the traditional budget. One of the well-established principles of our system of Government is that Parliament has the control of the purse and that taxes cannot be imposed or money spent without its approval. The annual budget is designed to secure Parliament's approval to the projected expenditure. It follows that the budgetary system has to be such as to ensure that the amounts voted

* Lord Bridges: The Treasury (p.188)

by the legislature under the several heads of expenditure are not exceeded and that they are not spent otherwise than according to the wishes of the legislature. The objective here is to ensure the financial and legal accountability of the executive to the legislature and, within the executive, to enable the formulation of similar accountability on the part of each subordinate authority to the one immediately above in the hierarchy of delegation.

(ii) Tool for Management - A budget may also be regarded as an operational document and, in that form, a valuable tool for management. The emphasis here is on programmes, activities and projects for which there is managerial responsibility in terms of cost, time and accomplishment.

(iii) Functional Approach - A classification on functional lines is sometimes advocated. This would enable all items of expenditure in a particular field to be grouped under one functional category, e.g., education, national defence, etc., irrespective of the department or the agency which actually incurs the expenditure. It is argued that this will help to give a clearer picture than at present of the aggregate of the Government's effort in each field.

(iv) Performance or Accomplishment - This is closely allied to the objective already discussed of the budget as tool of management with the emphasis shifted from cash to cost and expenditure to achievement. The concept and technique of performance budgeting have been developed in the U.S.A. and in a few other countries. As already stated, the

applicability of performance budgeting to our own conditions has formed the subject of study by one of our Working Groups. Our own recommendations are set out in Chapter III.

(v) Correlation with Plan - In the context of the planned economy of a developing country, the term 'accountability' has a broader connotation than in its ordinary usage. It is not concerned merely with the verification of due sanction and approved purpose for expenditure incurred by the relevant authorities. It extends to ensuring that the annual programmes and achievements are set out and implemented in terms of the long term Plan and its goals. Annual accountability remains but is part of a long term responsibility for executing the Plan.

(vi) Economic Analysis - In recent years, emphasis has been increasingly placed on the development of a proper system of budgetary classification of government transactions from the point of view of economic analysis. The budget, it is argued, should bring out the impact of the incomings and outgoings of a government on the behaviour of the national economy as a whole. It should enable a determination of how much of the national income has its source in government activities and what the extent of capital formation and asset creation is as a result of governmental operations. In setting out the

budget data, therefore, account should be taken of significant economic categories, such as consumption expenditure, transfer payments, capital investment etc.

(vii) Instrument of fiscal policy - In one of its most important aspects, the budget is a tool of fiscal policy, i.e. an instrument for consciously influencing the economic life of the community. The levels of taxation and expenditure which are regulated through the budgetary process are among the main devices for pursuing desired aims such as the development or stabilisation of one or more sectors of the economy. This indeed is not an isolated objective so much as a characteristic of the modern budget itself in so far as it makes an automatic contribution to the nation's fiscal policy.

2.4 To sum up, besides being the most important annual item on the agenda of Parliament, the budget serves a number of purposes, fiscal, financial and economic, administrative, managerial and developmental, in terms of each State and of the country as a whole. It is a document for parliamentary action and an instrument of parliamentary control. It is a management tool and a basis for administrative delegation. It sets out a programme of development and enables the adjudgement of performance. These objectives are not mutually exclusive. But, if there is one over-riding need today it is that all governmental processes - including the budgetary process - should be oriented to action and performance:

action that achieves optimum results, and performance that involves not more than reasonable cost, effort and time. The next Chapter accordingly deals with Performance Budgeting.



CHAPTER III

PERFORMANCE BUDGETING

3.1 Performance budgeting is essentially a technique of presenting Government operations in terms of functions, programmes, activities and projects. By means of this classification, the individual items which make up the budget are sought to be shown not only in financial terms but, as far as possible, in physical terms as well.. As observed by the Hoover Commission in their first (1949) Report "such an approach would focus attention upon the general character and relative importance of the work to be done or upon the service to be rendered, rather than upon the things to be acquired, such as personal services, supplies, equipment, and so on. These latter objects are, after all, only the means to an end. The all-important thing in budgeting is the work or the service to be accomplished, and what that work or service will cost."

3.2 Among the purposes sought to be served by performance budgeting, the following are the most important:

- (a) to present more clearly the purposes and objectives for which the funds are sought and to bring out the programmes and accomplishments in financial and physical terms,
- (b) to help a better understanding and better review of the budget by the Legislature,
- (c) to improve the formulation of the budget and to facilitate the processes of decision making at all levels of Government,
- (d) to enhance the accountability of the management and at the same time to provide an additional tool to management for control of financial operations, and
- (e) to render performance audit more purposeful and effective.

3.3 Though the technique has great potentialities, it is not without limitations, the more important one being its restricted value in respect of activities and governmental operations that are not measurable in any precise manner, as for example, law and order, external affairs and research. Also, it enables only a quantitative and financial evaluation

of programmes and activities; qualitative evaluation is beyond its scope. Again, the success of the technique depends upon the existence of well-organised departments and organisations identifiable with definite programmes and activities. In actual practice, however, a complete congruence of functions, programmes and activities with organisational units is not easy to achieve. These limitations, though substantial are, in our opinion, outweighed by the advantages mentioned earlier.

3.4 For concrete illustrations of performance budgeting, as well as for a detailed treatment of other aspects of the subject, we would invite a perusal of the Report of the Working Group on Performance Budgeting (included in Volume II of this Report). The Working Group propose the adoption of this method of budgeting in a phased manner. We endorse their main conclusion and recommend that performance budgeting be introduced at an early date. It should, however, be a gradual process extending over a few years. A review should be undertaken after a reasonable interval

in order to assess the progress made and consider the further extension of performance budgeting. It is, of course, necessary that adequate preparatory steps should be taken for the introduction of the system. We endorse the Working Group's suggestions in this connection. The following among other steps have been recommended by them;

- (i) The Finance Ministry should assume responsibility for introducing the system and coordinating the stages.
- (ii) In the phased application of this system both at the Centre and in the States, priority may be given to departments and organisations which are in direct charge of programmes or activities (developmental or other) involving large expenditure.

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(iii) The analysis of the functions, programmes, etc. of the departments selected may, as suggested by the Working Group, be entrusted to a team consisting of officers drawn from the Ministry of Finance, the administrative Ministry concerned and the Management and Administration Division of the Planning Commission. In addition we would suggest that an officer of the Audit Department might also be associated with this team.

(iv) A suitable training scheme may be devised for those who, at different levels, will be concerned with the introduction of the schemes;

and a manual prepared as soon as practicable.

- (v) Appropriate changes in the accounting system would be needed to meet the requirements of performance budgeting. These aspects have been analysed at some length in the Report of the Working Group. Detailed recommendations on this subject are, we understand, being made by the Study Team on Audit and Accounts.



CHAPTER IV

THE FINANCIAL YEAR

4.1 There was one successful effort, followed over the decades by many unsuccessful ones, to change the Indian financial year. And the centenary of the successful effort, if it were to be celebrated, would fall exactly in the current year, 1967. For it was in 1867, and beginning with the budget for 1867-68, that the financial year which had previously been from 1st May to 30th April was changed in conformity with the British practice to one commencing on 1st April and ending on 31st March. Second thoughts supervened almost immediately. But they proved ineffectual. Once every ten years or so thereafter and more recently as an almost annual feature, different suggestions have been made from different quarters for a change in the financial year. Before summarising these it might be useful to indicate the practice obtaining in other countries. This is as varied as there are quarters in the calendar. In other words, 1st April, 1st July, 1st October and 1st January are all pressed into use for marking the commencement of the financial year.

4.2 We may first illustrate from some of the countries of the East. In Japan and Iraq, as in India, the financial year begins on 1st April. In Pakistan the date of commencement has been changed from 1st April to 1st July. In Burma and Ceylon, it is 1st October. (It is interesting to note in this context that, in many

parts of India, the indigenous financial year starts at Diwali, i.e. somewhere in October-November). In China it is 1st January.

4.3 In the U.K., Ireland, New Zealand, South Africa, Germany and Denmark the financial year starts on 1st April. (So also in Canada, where however, it had undergone successive changes: 1st January, thereafter 1st July and now 1st April). In the U.S.A. it is 1st July; so also in Australia, Norway, Sweden and Italy. In France, Belgium, and the Netherlands, in Finland and in Russia, it is 1st January; so also in several of the South American countries, including Argentina, Brazil and Chile.

4.4 To resume the account of the efforts to change the Indian financial year, it may be mentioned that the first review was made by the Secretary of State as early as in 1870, i.e. only three years after the change had been effected. The question of revision continued to be raised thereafter. For instance, it was mooted by the Welby Commission in 1900. But the Government decided not to make any change at that stage. The matter was again raised in 1913 by the Royal Commission on Indian Finance and Currency (generally known as the Chamberlain Commission) who, referring to the need for more accurate budgeting, observed as follows:

"The revenues of India, whether shown under railways or customs or directly under the head of land revenue, fluctuate to an extraordinary extent with the success or failure of the agricultural operations of each year, and these again depend predominantly on the south-

4.5 The subject once more became a live issue after Independence. It was taken up for consideration in 1954 at the instance of the Prime Minister who referred to a non-official resolution brought before the Congress session at Kalyani asking for the financial year to commence from 1st July. The matter was examined again and the considerations which weighed with Government in rejecting the proposal for a change were as follows: Firstly, although the south-west monsoon was the principal monsoon, substantial areas depended for their prosperity on the north-east monsoon; and if 1st April by-passes the former, 1st July by-passes the latter; indeed no date could claim all-round suitability from this point of view. Secondly, the convenience of the members of the Legislature, which was one of the grounds urged for a change, could be provided for by adjusting the legislative programmes in such a way that the members got sufficient time to tour their constituencies. The question was raised again at the meeting of the National Development Council held in 1956. Among the Chief Ministers who pressed the desirability of a change were those of U.P., West Bengal and Kerala. The decision was once more in favour of the status quo. An additional argument was that any change in the financial year would necessitate changes in the assessment years of companies for purposes of income-tax and corporate tax and cause dislocation all round. Subsequently, the Estimates

west monsoon which spreads over the Indian continent and Burma in the months of June to October. Under present arrangements the Indian budget is presented before the end of March, and the Finance Member accordingly has to prepare his estimates in ignorance of the most important factor on which the results of the year will depend. The late Finance Member of the Viceroy's Council, indeed, has described the framing of a budget as a gamble in rain. We would observe, however, that the description applies only because the budget is taken before the monsoon. It is clear in fact that from the financial point of view the present date is almost the most inconvenient possible for the budget, and the suggestion has therefore been made that the date of the beginning of the financial year should be altered from the 1st April to the 1st November or 1st January."

This suggestion, viz., that the financial year should commence from 1st November or 1st January, was commended by them to the Government of India for consideration. The First World War broke out in 1914 and the consideration was postponed. The question was taken up again in 1921 on the suggestion of Sir Dinshaw Wacha, who advocated the adoption of the calendar year for the closing of accounts. The Government of India thereupon consulted the Provincial Governments, the Chambers of Commerce and other bodies and in their circular letter dwelt at some length on the advantages and disadvantages of the proposal. The Provincial Governments were almost unanimously opposed to any change, while commercial opinion was divided. In view of this, the Central Government dropped the proposal for a change. The matter was raised again in 1926 and in 1927 by members of the Legislature, but without much success.

Committee of the Second Lok Sabha in their 20th Report (1958) recommended that the financial year may commence from 1st October. The question has since then come up on more than one occasion. The latest is that, in their draft outline of the Fourth Plan, the Planning Commission have suggested that a fresh examination be made in the light of present needs.

4.6 It would be useful to set down briefly at this stage the reactions of the representatives of the several State Governments with whom we had an opportunity of discussing this subject. The representatives were in all cases senior officers of the Governments concerned and in most cases their Finance Secretaries. We must mention, however, that the opinions did not necessarily represent the considered view-points of their Governments. Moreover, since the discussions for the most part took place in January, 1967, the views in question would in no way be attributable to the present Governments of the States. Even so, it is of great interest to classify the points of view expressed and to analyse to such extent as possible the reasons underlying them. With the reservations mentioned above, it may be said that four State Governments, viz., Madras, Mysore, Punjab and Jammu and Kashmir (the last two in their written replies) were definitely in favour of retaining the status quo. All of them were of the view that

there was no particular advantage to be gained by disturbing it. If, however, a change was in any case to be made, Madras was in favour of 1st July, while Mysore was undecided as between 1st January and 1st July: the former seemed preferable for arriving at a better forecast of revenues, whereas the latter, in their view, would facilitate better execution of programmes. Of the States which made positive recommendations for a change, the largest single number were in favour of 1st July. These were Maharashtra, Uttar Pradesh, Kerala, Assam and Orissa. (West Bengal, represented by different officers, put forward three alternatives, viz., status quo, 1st July and 1st October.) Three States favoured 1st October; these were Madhya Pradesh, Gujarat and (with the 1st November also as an alternative) Andhra Pradesh. The last-mentioned State pointed out that in Indian conditions the traditional financial year beginning at Diwali or thereabouts would be the most appropriate. The two States in favour of 1st January were Rajasthan and Bihar.

4.7 The reasons urged by the State representatives in favour of the different alternatives may now be briefly indicated. It was clear that the four considerations foremost in the minds of the officers were:-

- (i) Accuracy of revenue estimates in the budget.
- (ii) Accuracy of expenditure estimates in the budget.
- (iii) Efficacy of performance.

(iv) Convenience of Legislators and Administrators.

Those in favour of the status quo in effect argued that no single alternative would secure all the advantages mentioned above even if this was considered from the point of view of any one particular State. Further, if any single criterion, e.g. accuracy of revenue receipts, was taken up and applied to different States, it would result in different dates being chosen for the different States for the commencement of the financial year; this was because, while the south-west monsoon was the most important for the larger part of the country, the north-east monsoon was significant for other areas and no financial year could be devised which did not straddle the two monsoons. In the result, it was thought by these representatives that there was no particular advantage in seeking a change in the present position. Asked specifically whether there need necessarily be uniformity in this matter (a) between the Centre and the States and (b) between the States themselves, the answer, almost invariably was that uniformity was certainly most desirable in both these contexts. If this is accepted - and we agree with the view expressed - the question of different States choosing different financial years (and the Central Government perhaps another) does not arise. We have to proceed on the basis of uniformity. Assuming then, that the Centre

and all the States will either adhere to the present position, or together choose one of the three alternatives available, the advocates of status quo urge that the balance of advantage lies in retaining it. This is because, apart from the merits of any particular alternative, the disturbance of the status quo is bound to result in some dislocation, small or large, in a number of respects: administrative, accounting and statistical. It is in effect pointed out that, other things being equal, there is an in-built reason for adhering to the status quo. The retention of the present financial year has also been supported by most of the Secretaries to the Central Government with whom we had an occasion to discuss this question.

4.8 The States which urge the adoption of the calendar year as the financial year argue that, after allowing for the time lag between estimates and presentation, it is only a budget presented on or about 1st January that can incorporate in its forecast of revenue the most adequate knowledge of the effects of the main monsoon. They also feel that a budget which comes into effect on 1st January, as compared with 1st April, cuts less into the working season available for the execution of schemes.

4.9 The emphasis of those who advocate 1st July, equally with those who favour 1st October, is on performance. In both cases, it is agreed that the working season is roughly from October to May and that there will be

dislocation if this period was broken up by the budget. Those who prefer July, however, are of the view that, after the sanction of the budget, two or three months should be allowed - not necessarily for the communication of budget provisions and appropriations - but in particular for the purpose of providing adequate time for all the preliminary steps associated with new works. These include callings for tenders, approval of contracts, ordering of stores and so forth. As distinguished from this, those who advocate 1st October urge the added advantage of utilising the monsoon months from June to August for the concluding stages of the preparation of the budget; the budget would be discussed towards the end of August and passed by the end of September. For one thing, as distinguished from a July budget, this would save both the budget staff and the legislators from having to devote the hottest months of the year to the preparation and discussion, respectively, of the budget. It has to be added that the sheer administrative job of timely communication of budget appropriations passed by the Legislature to the authorities in charge of execution at the field level is reportedly a problem for certain States and (according to their account) not a serious matter at all for other States. Those for whom it is a problem would prefer 1st July, because it could then be assured that by October - when

work would be started - all sanctions would have percolated to those in immediate charge of execution. The States which do not regard this as a problem are on the whole inclined to prefer 1st October, except where they consider it desirable to provide for a time lag for tenders, contracts, purchases etc.

4.10 We may now try to sum up briefly the relative advantages of the different alternatives in the light of the criteria enumerated in para 4.7:

(i) Accuracy of the revenue estimates in the budget:

Agriculture and therefore the monsoon - especially the south-west monsoon - is still important, though not as important as in the past, from the point of view of revenue estimates. This is true of the Central Government to the extent, for example, that many excises - and so too many export duties - are based on agricultural commodities such as sugar, tobacco, tea and jute. It is also true of the sales taxes of many States. But if what was at issue, however, was land revenue, one has to take note of its dwindling significance in the total size of the State budget. With these reservations, it may be said that for accuracy in this context:

- (a) the most suitable date is 1st January, while 1st October, is only slightly less so.
- (b) 1st April is the least suitable, while 1st July is only slightly better.

(ii) Accuracy of expenditure estimates in the budget:

A preliminary point is whether severe drought, and.

acute food shortage resulting therefrom, should or should not hereafter be regarded as features likely to recur fairly often. If the answer is in the affirmative, then this becomes one of the principal causes of expenditure both at the Centre and in the States; and the monsoons, especially the south-west one, become very important. In that event, again, as in (i) above, the most suitable budgets are those commencing on 1st January or, as the next priority, 1st October. Also, 1st April would be the least suitable and 1st July only slightly better.

But if severe droughts are to be regarded as an exceptional feature on which normal budgetary arrangements need not be based, there would have to be an entirely different angle on accuracy in expenditure estimates. This would then depend, firstly, on the extent to which the budget estimates are based on knowledge of the revised estimates of the current year, and secondly, on how far the available revised estimates cover that part of the working season which falls within the current budget year. Since the working season is October-May and since three to four months have usually to be allowed for in order that current data may influence the next year's estimates, it seems clear that the best budget from this point of view is that which begins from 1st October. Next in order of priority would be 1st July. The worst would be 1st January, while 1st April would be

be slightly better.

(iii) Efficacy of performance:

The efficacy is in terms of what is done or not done by officers in the field. This has to be considered for different categories of works:

- (a) New works, for the first time provided for in the budget.
- (b) Continuing projects only partly completed during the current year and in fact expected to be only partly completed; and for which therefore a budget provision has been made for the next year.
- (c) Individual projects expected to be completed during the year which is current and therefore not figuring in the budget, but which nevertheless, for unforeseen reasons, have not been completed and would therefore be carried forward to the next year; and
- (d) Continuing works (e.g. road maintenance) for which no line can be drawn between one budget and another, and provisions for which invariably continue from budget to budget.

This categorisation is important because it has a bearing on factors which hinder or facilitate performance:

Category (a): raises the question both of preparatory steps (contracts, stores etc.) and the communication of budget grants to the

executives in the fields. We are, however, of the view that the preparatory steps in question are not a serious or universal problem. Further, it is only in exceptional cases that as many as three months would be required for the completion of these steps.

Category (b): raises only the question of the communication of budget grants. Where the system of communication operates efficiently, there should be no dislocation of work on account of an apprehended "lapse of grants".

Category (c): involves greater difficulty. The field authorities have to be assured that they can go ahead even though there is no budget provision; and before giving such an assurance the higher authorities have themselves quite often to seek the sanction of the Finance Ministry (for a possible supplementary demand etc.). Any budget year - or any budgetary or administrative arrangement - which tends to increase the number of instances in category (c) is obviously not desirable from the point of view of performance.

Category (d): usually presents no difficulty, provided the system of communication of budget

grants is tolerably efficient. Moreover, it is in regard to this category of works that most field officers feel confident that they can proceed with the work without undue risk of later incurring the displeasure of authority.

Taking a total view of these categories and giving due weight to the more difficult ones - since these are the weak points in execution - we feel that, from the point of view of efficacy of performance, 1st October and 1st July are equally suitable. The least suitable date is 1st April, while 1st January is only to some extent better.

(iv) Convenience of Legislators and Administrators:

This may be looked at from two angles:-

(a) suitability from the point of view of presenting and passing the budget; and

(b) suitability from the point of view of a legislator who desires to be in touch with his constituency.

So far as (a) is concerned, the least suitable alternative seems to be 1st July since the budget would have to be prepared and passed in the heat of the summer; none of the other dates is open to much objection, though 1st January would probably be the most congenial, while 1st April on the one side and 1st October on the other would not come far behind, each having something to commend it.

As regards (b), the desideratum would be for the legislator to be as free as possible to tour his constituency - and for the administrators to attend to their other duties - during the fair season, i.e. October to May. The arrangement that would best ensure this would be a budget that comes into force on 1st July or 1st October. Neither 1st January nor 1st April would be suitable from this point of view.

4.11 We have thought it desirable to analyse at some length the various criteria which - not always explicitly - are in the minds of those who advocate one or another alternative for a change in the financial year as well as of those who urge a continuance of the status quo. The alternatives are several and the criteria to be applied many. The conclusion one may reach is, in the last analysis, a matter of priorities. Should the accent be on the efficacy of performance or the accuracy of revenue budgeting? On the convenience of legislators or the accuracy of expenditure estimation? Since no one solution reconciles all these, what particular balance of advantage should be regarded as justifying a disturbance of the status quo with its attendant disadvantages? We have considered these questions and feel that if the status quo is to be changed, the balance of ^{of} advantage would lie in favour of 1st October, more especially from the point of view of performance on which we lay

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emphasis throughout this report.



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CHAPTER V

BUDGET ESTIMATES

5.1 Sound budgeting involves, among other things, sound estimating. The soundest estimates - whether of receipts or expenditure - may in the event turn out to be not wholly accurate. But they should not be avoidably inaccurate. In other words, the estimates should be arrived at by applying as scientific methods as possible to as up-to-date data as obtainable. The constant improvement of both these factors - methods and data - is of great importance. For instance, the criticism is sometimes made that there is a tendency to under-estimate revenue receipts and over-estimate expenditure. One consequence of such "conservative" budgeting, it is pointed out, is unnecessary taxation. Method and data will enable budget-makers to steer the middle course between too much caution and too great an optimism. We understand that so far as revenue estimation is concerned, the Board of Direct Taxes and the Board of Central Excise and Customs have been taking measures for the improvement of the system generally, as well as ^{of} the procedures relating to individual items or groups.

5.2 In response to a suggestion made by the Public Accounts Committee, the Board of Excise and Customs have also taken preparatory steps for the reorganisation

of their Statistics and Intelligence branch. Executive instructions have been issued for taking into account all the relevant factors like the starting of new factories, the expansion of the existing units, the availability of raw materials, the conditions of agricultural crops and changes in the pattern of consumption, production etc. in the preparation of estimates.

5.3 Different methods are employed, singly or in combination, for forecasting revenue. Under one of these, the rule of the penultimate year, the revenue estimates for the budget year are based (with necessary modifications) on the actual revenues for the fiscal year last ended. For instance, in preparing the revenue estimates for 1967-68 the figures of actual revenue used would be those pertaining to 1965-66, which is the last completed year for which such figures are available. Another technique, known as the method of averages, takes as the basis the average of a three-year or five-year period that has preceded. A third method is that of "direct valuation" where the emphasis is shifted from the past figures of revenue to all such current economic data - e.g. production, prices, consumption, export, etc. - as will make possible an assessment of the relevant trends, during the budget year and, on the basis of those trends enable direct estimation of revenue receipts under the particular major head of revenue.

5.4 These methods are not mutually exclusive and each has its place in the scientific forecasting of revenue. The last is the most comprehensive, but depends for its success on the coverage and accuracy of the statistics available. We recommend that the two Boards review, from this angle, the adequacy of the statistical data now available to them and take measures to supplement them where necessary.

5.5 Several factors contribute to the inaccurate forecasting of expenditure, which usually takes the shape of overestimation. Mention may be made of some of them:

(1) Over-estimating is partly due to psychological reasons. First, there is undue optimism as to how much can be executed (and therefore how much can be spent) during the course of the year. Second, there is often an apprehension - usually born of past experience- that the departmental figure is likely to undergo pruning at some stage or the other during the long budgetary process and must, therefore, be pitched high enough to allow for the probable reduction.

(ii) There are certain departmental formalities which are time-consuming. There is delay, sometimes extending over several months, in the issue of formal sanctions to the schemes or projects owing to the time taken in obtaining clearance from the Finance Ministry. Then there are

procedural delays all along the line: for example, the procedure regarding the industrial licensing, clearance from the indigenous angle from the Directorate General of Technical Development, clearance from the Capital Goods Committee, the Chief Controller of Imports and Exports, the Central Water and Power Commission, the Planning Commission, etc. There is also delay in communicating the sanctions to the Project authorities from the various intermediary levels. All this results in substantial deferment of execution and therefore considerable under-spending.

(iii) Expenditure estimates sometimes go awry because of the default of contractors or of suppliers of plant, machinery or equipment. Though the completion or delivery dates are specified in the contracts and provision is usually made for a penalty in the case of failure to complete the work or deliver the goods on these dates, delays often occur on the part of contractors as also of suppliers, both indigenous and foreign. Some of the causes of delay are beyond the control of the contractors and suppliers; but quite often the delay can be traced to wholly avoidable reasons.

(iv) An important cause of delay is the procedure involved in obtaining the releases of foreign exchange.

5.6 Some of the factors we have mentioned above -

as underlying either delay in execution or inaccuracy in budgeting - are inherent not so much in the administration, as in the situation generally. For them, therefore, no administrative remedy is really applicable. But there are a number of administratively avoidable factors which contribute to both delay and inaccuracy. There can and should be an attempt at all levels to counteract them. Our suggestions are two-fold:

(i) We consider that managerial techniques such as PERT (Programme Evaluation and Review Technique) and C.P.M. (Critical Path Method) should be introduced as early as possible in Government projects and Government Departments, especially those concerned with the execution of relatively big schemes. Among other things, the adoption of these methods should lead to a much larger measure than at present of calculated control over points of crucial delay - to the extent such points are controllable - and, in the same process, to a much more reliable estimate than now obtains of the twin factors of time and expenditure.

(ii) We elsewhere suggest that administrative Ministries should assume near-autonomous control over their own budget grants, this in turn implying much greater individual responsibility than at present of the Department or Ministry concerned in regard to the framing of its own budget. This responsibility cannot be discharged

unless each such administrative organisation - Ministry, Department or Office - has, where its size justifies this, a well-equipped Budget Cell with a minimum of financial and accounting officials trained in conventional and performance budgeting. When these Cells begin to operate in the manner envisaged, one of the results should be a very large reduction in that type of over-estimation of expenditure which is traceable to out-of-date data, imperfect techniques and, lastly, inadequate familiarity with the practical aspects and vicissitudes of the schemes and projects for which estimates are framed.



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CHAPTER VI

BUDGET IN PARLIAMENT

6.1 We may now consider some of the procedures in Parliament in so far as they concern the Budget. One point that is sometimes urged is that ways and means should be devised for providing fuller opportunities to the members of Parliament to discuss the budget and make an effective contribution to the policies underlying the budget provisions. To this end, many suggestions have been made from time to time.

6.2 One proposal is that the Standing Finance Committee, which had been abolished in 1952, be revived. The 20th Report of the Estimates Committee (Second Lok Sabha - 1957-58) puts the case for the revival as follows:-

"It might be a distinct advantage both to Government and Parliament if this Committee is revived. It might have the authority to scrutinise such new items of expenditure above a certain limit as the Government might place before it before they are included in the Budget. The Committee might, however, be purely advisory and Government need not be bound to accept all its suggestions or its criticism. Even then it would provide an opportunity to members of Parliament to study the problems in their proper perspective and thus enable them to offer well-informed criticism on individual schemes in a manner which cannot otherwise be in the Parliament. Besides, this also would enable public participation in the drawing up of the schemes for inclusion in the Budget."

The suggestion was not accepted by Government, who felt that the situation had materially changed after Independence. As in the British system, the executive was now fully

responsible to Parliament, and Parliament itself had numerous opportunities of discussing important policy matters as well as important executive decisions. On careful consideration, we feel that the question of the revival of the Standing Finance Committee need not be pursued.

6.3 Another suggestion which is sometimes made is that, as in the United Kingdom, the budget could be discussed by a Committee of Supply into which the whole House would convert itself while performing this duty. The advantage urged is that the procedure would be much more informal than if the House was in session as Parliament. Our view is that discussions in Parliament are not, as it is, unduly restrained by formality and that the device of a Committee of Supply would be an unnecessary refinement.

6.4 Another point urged for consideration is whether the number of days allotted for discussion of the budget proposals by the House might not usefully be increased. The budget is presented to the Legislature on the last day of February and the whole process from the presentation of the budget to the passing of the Appropriation Bill is gone through during a period of nearly two months. There is no reason to consider this too short a period if the emphasis is, as in our opinion it ought to be, on the prompt execution of the budget no less than on its adequate discussion. Any device which has the effect of putting off to a late date the sanction of budget grants, and thereafter

the communication of such grants to the executive levels would be retrograde from the point of view of performance. While, therefore, we feel that the passing of the budget should not be delayed beyond what obtains under the prevailing procedure, we would at the same time point out that the allotment of more time for discussion, if that is thought to be necessary, can be provided by Parliament by suitable regulation of its internal business.

6.5 One reform may be suggested. The discussion on a demand is usually more informed and purposeful if initiated by the Minister concerned and if, in his introductory remarks, he explains the policies underlying the estimates, the physical programmes planned, the performance, if any, during the preceding year and so forth. The practice which we now commend was in fact recommended in the past by the Estimates Committee. It is understood, however, that it has not been generally adopted. We would recommend that it be made the invariable rule.

6.6 We deal elsewhere with the control of expenditure by Parliament (and State Legislatures) through the machinery of their own committees - such as the Public Accounts Committee - and on the basis of the Audit Report, the Appropriation Accounts and the Finance Accounts (prepared separately for the Union and State Governments) by the Comptroller and Auditor General. We propose here to make one or two other suggestions.

6.7 The duty of presenting a report on the accounts of the Union and the States has been laid on the Comptroller and Auditor General by the Constitution, while other instructions lay on him the obligation of presenting the Appropriation accounts and Finance accounts to the Governments concerned. While the executive instructions provide for the Comptroller and Auditor General submitting the Appropriation and Finance accounts on such date as he may with the concurrence of the Governments concerned determine, no such stipulation has been made in the Constitution with regard to the submission of audit reports on these accounts. In the Constitution of a number of countries, however, there are provisions prescribing the dates by which these reports are to be submitted by the Comptroller and Auditor General to the Treasury or to the Legislature. In India also the question of submitting by a prescribed date the Appropriation Accounts, Audit Reports etc., by the Comptroller and Auditor General has been raised in some State Legislatures, but in the absence of specific provision in the Constitution the question was not pursued further. Similarly, some cases of delayed submission of these documents by the State Governments to their respective Legislatures have also arisen in the past. It is, in our view, desirable that specific dates should be fixed by which the Appropriation Accounts and Audit Reports should be submitted - (a) by the Comptroller and Auditor General to the Finance Ministry; and (b) by the Finance Ministry to Parliament. We

recommend that a provision to this end should find a place in the Bill governing the functions & duties of the Comptroller and Auditor General which is under the consideration of Government. We would further suggest that the Comptroller and Auditor General should be required to forward his report to the Finance Ministry by a definite date, say, 15th January and the latter to submit it to Parliament by 31st January. These suggestions apply mutatis mutandis to the State Governments and Legislatures also.



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CHAPTER VII

BUDGET, PLAN AND ECONOMIC ANALYSIS

A. CORRELATION BETWEEN THE PLAN AND THE BUDGET

7.1 At present there is a lack of correlation between the development heads in the Annual Plan and the budget heads. This applies to both the Central budget and the State budgets. The outlays under the Plan are exhibited under the heads of development prescribed by the Planning Commission, while in the budget all items of expenditure are shown according to the heads of account prescribed in consultation with the Comptroller and Auditor General. Although the expenditure on the Plan schemes is exhibited separately in the budget, the development heads adopted in the Plan are at variance with the major heads adopted for budgeting and accounting purposes. Besides, the expenditure on various Plan schemes under a head of development is reflected in the budget under more than one major head falling under the Revenue Account, the Capital Account and also under Loans and Advances. This lack of direct correlation between the Plan and budget heads not only renders it difficult and cumbersome to follow with real understanding the financial provisions made in the budget for Plan schemes, but in relation to schemes in State Plans gives rise to special problems in the matter of regulating Central assistance. For these reasons, it

is necessary to bring about better integration between the account heads of the budget and the development heads of the Plan, keeping in view all the relevant considerations.

7.2 There is another important factor which emphasises the need of a better nexus between the account heads of the budget and the development heads of the Plan. Under the existing procedures the release of Central assistance to the States in respect of Plan schemes is regulated on the basis of departmental figures of expenditure incurred under different heads of development. But the final adjustment of such assistance has to be done on the basis of audited figures of expenditure. For this purpose, it is essential for the Audit authorities to have before them (a) a statement of approved schemes included in the annual plan of the State, (b) particulars of the provision made for agreed schemes under the various budget heads of accounts and (c) the actual expenditure incurred under each of these heads. Similarly, whenever any changes in the plan schemes are made during the course of the year, a list thereof would need to be supplied to the audit. It is, therefore, necessary for the purposes of final determination of Central assistance, that a proper link should be established between the budget heads of account and heads of development.

7.3 An important principle of classification of Government transactions is, however, that the heads of account should correspond to the Departments concerned with the

raising of revenue or the incurring of expenditure. The provision for a particular scheme is made in the budget estimates,--and the expenditure thereon is debited to the grant--of the department in charge of the schemes irrespective of the head of development in the Plan. In view of this accepted principle, it is not practicable to recast the budget completely in terms of the development heads. What can, however, be attempted is a greater measure of uniformity in classification. This involves the modification of some of the existing minor heads, sub-heads and detailed heads - or in some cases the opening of new ones - to harmonise with the Plan heads of development. Another suggestion in this connection is that the existing heads of development should be placed (with slight modifications) below the revised functional groupings and the related major heads put under the various heads of development. Both these suggestions would involve a number of modifications in the existing major heads of accounts. We suggest that the position be reviewed in consultation with the Comptroller and Auditor General and such changes introduced as are appropriate and practicable.

7.4 After a consideration of the various alternatives, it appears to us that the best way of bringing the accounting heads and development heads in line with each other would, under the existing structure of accounts heads, be to provide a link between the Plan schemes and the budget provision by way of a supplementary exercise through the publication of a separate Plan-Budget linking document

by each State Government. This document would contain a statement of schemes included in the Annual Plan, arranged under heads of development indicating the provisions made for each of the schemes under the various budget heads of accounts. The link between the Plan schemes and the budget heads could be provided, for instance, by means of code numbers to be assigned to each scheme. Such a system could be put to use at the stage of the formulation of the budget documents; it would facilitate not only the correct booking of expenditure but also proper accounting and reporting and would enable a regular track being kept of the expenditure under a particular head of development. In this connection, the system adopted in Uttar Pradesh is worth mentioning. The procedure followed by that Government is indicated in brief in the note at the Annexure to this Chapter.

7.5 The suggestion made by us in the preceding paragraphs is based on the assumption that the existing systems of accounting and budgeting will, in the main, be retained. We would, however, invite a reference to Chapter III of this Report, wherein we have recommended the introduction of Performance Budgeting. Certain recommendations in regard to the linking of the heads of development under the Plan with the budget and accounts heads have been made in the Report of the Working Group on Performance Budgeting.* A definite view has been expressed therein that the problem can be successfully tackled only if changes

* Please see Volume II of this Report.

both in the heads of accounts and in the heads of development and the groupings of schemes thereunder are brought about. In the opinion of the Working Group, the heads of development need to be recast so as to reflect the collection of homogeneous groups of schemes; and this should be done in such a manner that the new heads of development and the grouping thereunder correspond to the major and minor heads of accounts as proposed to be revised under the proposals of Working Group. We consider that the acceptance of the changes proposed in the heads of account and development heads will help bring about a better correlation between the budget and plan documents.

B. BUDGET AND ECONOMIC ANALYSIS

7.6 An economic classification of Government transactions is largely useful at the stage of policy formulation as it enables the policy makers to review broadly the pattern of allocation of resources and its impact on the rest of the economy. An economic classification also provides a direct link with the national accounting data since it provides the necessary material for the construction of such an account with reference to the public sector. It is thus essentially an application of the national accounting techniques to the transactions of the Government sector. The object of such classification is to express the receipts and expenditures of Government in terms of categories meaningful for the purposes of economic analysis and to highlight the relationship which they bear to similar categories in other sectors of the economy.

7.7 In the developing countries, the need for an economic classification of Government transactions has arisen primarily on account of the fact that the public sector has come to occupy a very prominent role in development plans, and the transactions of the Government sector constitute a significant proportion of those of the entire economy. As a result, the need of reclassifying Government transactions in order to make the budget a more effective instrument of economic policy has come to receive increased attention. Moreover, in a country like India where the national income data are not adequate, the economic classification of the Government transactions has also to be viewed as an essential step towards the construction of a comprehensive system of national accounts. This is needed not only for a better understanding of the functioning of the economic system but also for making necessary projections of savings, consumption and investment in the context of development plans.

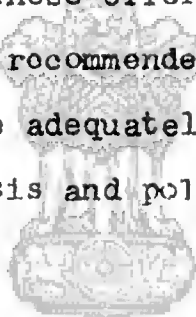
7.8 The need for such classification arises because all Governmental transactions do not have the same economic significance in the sense of having the same impact on the economy. Different items of importance in the budget which have a different significance from the economic point of view have to be regrouped for this purpose. It is with this aim that the Ministry of Finance has been bringing out an economic classification of the Central Government budget since 1957-58. The main utility of this exercise is that it promotes a better understanding of the

economic impact of the Government's operations. However, for a proper appreciation of the Government's role in the generation of incomes, savings and capital formation, it is essential that this technique is also extended to the budgets of the State Governments and the financial operations of the public sector undertakings run either as companies or as statutory corporations. A few of the State Governments, e.g., Punjab, Madhya Pradesh and Orissa, bring out an economic classification of their State budgets. To be really useful, this approach must not only be extended to budgetary transactions at all Governmental levels, but also to non-departmental enterprises of both the Central Government and all State Governments.

7.9 A serious lacuna in the 'economic classification' at present is that it is presented in a supplementary document and has no specific role in the formulation of the budget or budgetary policy as such. Since the budget has an increasingly significant role to play in the regulation of the economy, it would be important that economic classification be integrated into the budgetary process itself. Such a process obtains in several advanced countries, e.g., in the U.K. and the U.S.A. It would be desirable that an economic analysis be carried out of the budget estimates of each department so that they could be analysed, at the time of aggregating the various demands, from the point of view of assessing the magnitude of expenditure in a particular year. We would, therefore, suggest that

to every Demand for Grant there should be attached an economic classification of that particular Demand.

7.10 The usefulness of the technique of economic classification has to be judged not only in terms of a better economic understanding of Government operations but also in terms of how far it facilitates policy formulation. The data in India in this regard are still deficient. For example, we have as yet no official series of savings and investment. We understand that on this and other important items the Central Statistical Organisation is making efforts to compile the data and construct the series. These efforts, which will be complementary to what we have recommended, should, in due course, help to fulfil much more adequately than at present the needs of economic analysis and policy formulation.



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ANNEXURE

The Uttar Pradesh Government publishes as part of its budget literature every year a brochure entitled "Annual Plan Analysed in terms of Budget". The purpose of the document is to establish, by a system of cross references, the correspondence between individual plan schemes and the different items under budget heads of accounts. The system operates by means of code numbers, one of which is assigned to each scheme. This may be made clear by an illustration :

Code number 1.1.1.01 would stand for the "Expansion Scheme for the Multiplication, storage and distribution of improved seeds, etc.". Similarly, 1.1.1.02 would be the code number for "Introduction of Hybrid Maize and Jowar seeds" under the group "Seed Farms" which in turn falls under the head of Development "Agricultural Production". The entire Plan Outlay is distributed over Sectors Nos.1 to 7 as follows :

1. Agricultural Programmes
2. Cooperation and Community Development
3. Irrigation and Power
4. Industry and Mining
5. Transport and Communications
6. Social Services
7. Miscellaneous.

The number 1 in the fifth digit from the right hand side, in both the examples given above, would stand for the sector "Agricultural Programmes". Thereafter, the code number in the fourth digit would represent the head of development under the various sectors, the third digit would indicate

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the grouping of schemes under a particular head of development and the first two digits from the right hand side would denote one of the large number of individual schemes listed in the publication. Thus, in the first case, the two digits from the right, namely, 01. enable the name of the scheme to be traced, the third digit indicates the grouping of the schemes which in this case is "Seed Farm", ^{and} the fourth digit stands for "Agricultural Production" which is the head of Development under Sector 1 (fifth digit from the right) which is "Agricultural Programmes". In the second instance the sector, head of development and group are the same as for the first; only the individual scheme is different and the relevant code number (.02) enables its being identified from the list. Lastly, we may consider the code number 1.4.1.14 - which stands for "Intensive Cattle Development around the Milk Shed area of Etah". The first two digits on the right hand side represent the serial number of the scheme. The third digit 1. indicates the grouping which is "Cattle Breeding". The fourth digit (4.) indicates that the scheme falls under the head of development "Animal Husbandry".

Finally, the fifth digit (1.) represents the sector entitled "Agricultural Programmes".

CHAPTER VIII

LAPSE OF GRANTS

8.1 All funds voted by the Legislature -- budget grants at the beginning of the year and supplementary grants during the course of it -- lapse when the financial year ends. The Executive must seek the sanction of the Legislature afresh for funds needed during the ensuing year, including those which had been expected to be spent before the 31st of March, but were not and which, therefore, lapsed. This is the "rule of lapse". More specifically it implies that no portion unexpended during the year may be reserved or appropriated by transfer to deposits or any other head, or drawn or kept in the cash chest, to obviate the lapsing of the grant and to be expended after the end of the year for which the grant was made.

8.2 The factors we have dealt with in Chapter V as underlying the over-estimation of expenditure are also relevant here as leading to the lapse of the unexpended part of provisions which ab initio were too high. But not all provisions are of this type. The estimates may have been quite sound, when made, but circumstances may have later intervened which interfered with the execution of the programme. Or the execution itself may be inadequate or put off till the last stages of the financial year. Further it must be remembered that provisions are, within

limits, interchangeable through the process of reappropriation. This process is governed by a set of rules; and imperfect understanding or inefficient implementation of these rules may lead to funds lapsing in one sector of activity which might have been used effectively in another sector. In all such cases the remedy is not to seek abolition of the rule of lapse -- that would be impracticable but to plan better, execute quicker and implement rules more effectively.

3.3 We may add that what we have said about the "abolition" of the rule of lapse equally applies to two other alternatives sometimes suggested, viz.

- (i) an 18-month or 24-month budget instead of a 12-month one, or
- (ii) a 15-month budget with the further refinement that the last three months of one budget overlap with the first three months of the next budget.

In the first case, the difficulties continue to exist; only they recur at longer intervals. The second course, if followed, would only result in present confusion being worse confounded; for obvious reasons, two sets of sanctions on the same set of funds -- in other words two budgets in our sense of the word -- cannot co-exist. In this as in many other matters, no budgetary formula or similar device can counteract the results of inadequate planning and inefficient execution.

8.4 The "rush of expenditure" towards the end of the year is an example in point. It is usually a symptom of bad execution and is sometimes the result of deliberate evasion of rules. The desire in either case is to avoid the lapsing of grants. A contributory factor sometimes is the apprehension that the non-utilisation of the budgeted amount would invite unfavourable comments from the authorities above and ultimately perhaps from the Public Accounts Committee. The worst cases of rush of expenditure are those where moneys are withdrawn and, in contravention of rules, are deposited elsewhere or nominally "paid" to a contractor who is yet to complete the work. Such instances when detected should be severely dealt with; we believe that proper investigation will reveal that cases of this type are by no means few. Hardly less excusable are the instances in which provisions for developmental or other schemes are used up towards the end of the year on items such as furniture not originally contemplated, merely for the reason that there is an unexpended budget provision at the credit of the Department or Office concerned. The intensification of legitimate activity in these particular months -- e.g., road-making for which February or March are among the most suitable months -- stands in a different category. In other words many types of items are covered by the general phrase "rush of expenditure" and these must be properly sorted out for purposes of remedial action where necessary.

8.5 Another aspect which calls for attention is the one we have alluded to as connected with the rules of reappropriation. Even though it is enjoined on the Ministries and other spending authorities to surrender the savings within a grant or appropriation as soon as the possibility of such a saving is known, it often happens that savings are withheld till the close of the financial year. Funds that could have been effectively spent elsewhere are thus uselessly locked up and the programme of the Government as a whole suffers on account of inefficient financial management.

8.6 As mentioned above, in spite of the repeated instructions of the Finance Ministry, instances persist of the Departments and organisations not surrendering funds in time. This may happen partly because executive authorities are not actually aware of the state of expenditure and the progressive total of the expenditure against their allotments. The remedy in that case would be to improve and streamline the accounting and budgeting arrangements - a point which is discussed elsewhere in this Report.

8.7 We recognise, however, that there is also a psychological factor behind the reluctance to surrender funds in time; and if the Ministries or Project authorities could be given some assurance, albeit informal, that under-spending in one year would not unduly prejudice the budget estimates for the next year, the Department's reluctance to surrender funds in time would tend to diminish. We

feel that it should be possible for the Finance Ministry to give the requisite assurance in this matter.

8.8 The lapse of funds for projects or capital programmes can also be reduced by improved managerial techniques and by a better phasing and programming of the expenditure on a project. The introduction of performance budgeting, which would relate the financial outlays to the physical accomplishments, should also help to reduce the incidence of the lapse of funds, since such lapses would be related to shortfalls in performance and would, therefore, be noticed without difficulty.

8.9 We have alluded elsewhere (in Chapter IV on the "Financial Year") to different categories of projects -- new schemes, continuing schemes expected to be completed in a particular budget year but not so completed and so forth -- each of which involves a somewhat different problem from the point of view of the lapse of the old provision and communication (or failure or delay in communication) of the new provision. A prompt system of communication of the new budget grants is obviously necessary in these as in all other cases. But, besides this, a part of the difficulty would be met by more liberal recourse to the system of Vote on Account. Funds by this means can be provided on a provisional basis. This is in fact done by the Central Government and no difficulties have been encountered.

CHAPTER IX

LUMP-SUM AND TOKEN GRANTS

9.1 It is a well-accepted principle of budgeting that no provision should be made for a scheme unless adequate details, together with a break-down of cost, have been furnished to the Treasury and accepted by it. In other words, lump-sum provisions, i.e., provisions of which the details have not been worked out and, therefore, are not available, should not ordinarily be included in the budget. This salutary principle has been repeatedly emphasized by Parliamentary Committees and the Finance Ministry. Equally often it has been passed over in practice by the administrative Ministries, with the Finance Ministry seemingly helpless to enforce it.

9.2 Substantially similar considerations apply to token provisions. There is, however, some difference. A token grant, as distinguished from a lump sum provision, is one of which the details are, or can readily be made, available; it is in fact a small or 'token' part of a larger demand which can be spelt out in adequate detail. The actual demand is confined to a nominal amount because the expenditure itself can be met by reappropriation from savings in other units of appropriation within the same grant. If, despite the feasibility of reappropriation, a demand is nevertheless placed before the Legislature, it

is because the item of expenditure is in the nature of a 'new service' and therefore requires the sanction of the Legislature irrespective of the source of finance. It follows that token demands can properly figure only in supplementary budgets. There can be no question of savings being available when the main budget is presented.

9.3 By a confusion of ideas, however, the term "token" demand is sometimes used as if it were interchangeable with certain types of demand for a "small" amount. To illustrate, we may take the instance of a big scheme for which the provision is expected to be spread over two or more years. If such a scheme is to start towards the end of a particular budget year, the provision necessary in that budget would be relatively small. This provision, or sometimes only a nominal amount, is included in the budget, is described (erroneously) as a 'token' provision and, on this basis, approval is sought for the scheme as a whole without disclosing adequate details of total expenditure. This is clearly wrong. On the subject of 'token' grants all that need be said, therefore, is that the strict meaning of the term should be kept in mind and such grants asked for only in the one particular context - which we have defined above - in which they are permissible.

9.4 As for lump sum provisions, logically there should be a total ban on their inclusion in the budget. It is sometimes argued that since it may not always be feasible to defer individual projects over a whole year, the

requisite funds would have to be found in the course of the year through supplementary demands. If these demands are many and large, they would between themselves constitute a "little budget" and may even involve mid-year taxation. As between mid-term budgets and taxation on the one hand and lump sum provisions on the other it is argued that the latter are much the lesser evil. We consider this a counsel of despair. We agree that it would be both facile and undesirable to admit large items of expenditure and put them before the Legislature at any odd time of the year. That would make nonsense of the whole notion of budgeting. At the same time it is surely not correct to speak as if the only choice ~~which~~ before Administrative Departments is between sending half-baked schemes punctually and properly worked out schemes unpunctually; in other words, that it is not possible to adhere to a time schedule, whereby schemes are submitted both in adequate detail for financial scrutiny and in adequate time for inclusion in the budget. We are of the view that the administrative Ministries can and should take steps to obtain the clearance of their budget proposals from the Finance Ministry well before the final date stipulated in the budget calendar. This involves scrupulous observance of the existing instructions. It also points to the advisability of staggering such proposals over a period instead of waiting till the last moment and then rushing them together to the Finance Ministry.

9.5 Lump sum provisions should be regarded as permissible only in the most exceptional circumstances, e.g., where urgent measures have to be improvised for meeting an emergency. They would also, in a limited sense and in relatively moderate amounts, be justified when a detailed break-down is not possible, as when preliminary expenses on a projected scheme, e.g., for survey, etc., can only be roughly guessed rather than estimated item-wise. In all other instances the proper course would be to insist on consideration being deferred until the next budget; in other words, to refuse to make provision in the proximate budget for schemes which have been inadequately or incompletely examined on account of not having been taken up for scrutiny early enough in the budget year. Where the scheme is so urgent that it cannot be deferred for a whole year, the proper alternative would be a shorter postponement together with full scrutiny meanwhile, and not that of waiving altogether the requirement that adequate details should be worked out. However, urgent a scheme, it obviously cannot be put into effect without the details having been properly set out. A postponement can, therefore, ordinarily do no harm; and, while the less urgent scheme gets deferred to another budget altogether, the more urgent one has a chance of being considered at the time supplementary demands are asked for in the forthcoming year, involving only a few months' postponement. If this selective approach is followed, there

CHAPTER X

REVIEW OF EXPENDITURE

10.1 Detailed instructions exist for the control of expenditure and the reporting of its progress. The rules contain general instructions relating to the responsibility of spending authorities at various levels. In addition, there are the departmental manuals containing specific and particular instructions to suit the nature of operations in each department.

10.2 It is necessary to take notice of the various inadequacies revealed in the actual operation of the present procedure and rules. The reporting is done in terms of expenditure and not also of physical performance. Even so, as a rule, at no given time up to a late stage in the financial year do the administrative Ministries or the spending authorities have up-to-date figures of the progress of expenditure; they have almost invariably to get the information from the accounting authorities who are officers of the Audit and Accounts Department. The Ministries and Departments enter sometimes into commitments in comparative ignorance of the progressive figures of expenditure or the availability of funds against the appropriations or allotments made. Moreover, not much use is made of the expenditure data in decision-making, including budgeting decisions, largely because the system does not provide for adequate and up-to-date data being

made available at any particular point of time as to what has been spent and what is available. When the figures of expenditure do become available it is usually too late for ensuring at the level of Department or Ministry either that the current appropriations are not exceeded or that the requisite amounts are provided in the next budget.

10.3 The primary purpose of progress reporting is to furnish data to the management periodically regarding the progress in the execution of programmes, physical accomplishments, manpower utilization and financial results. The object of such reporting is to enable the various management levels to monitor the operations that are included in their respective jurisdictions and to enable a systematic appraisal and evaluation of the work done. A good system of progress reporting should provide a basis for a comparison of the current progress against the past and the projected schedule of work. Specifically, in so far as the system of reporting the progress in expenditure is concerned, the object may be stated as under :

- (i) accounting data should facilitate the formulation of a policy and also throw up material that will make possible the assessment of the working of the policy, and
- (ii) it should also render the action of each agency accountable to the higher agency or to the Legislature and through it to the public in the ultimate analysis.

10.4 ~~At present~~, expenditure reporting is done with reference to the major and minor heads of accounts. Such an emphasis limits its capacity to facilitate a comparison of the progress in expenditure with the progress in physical terms. This is particularly so in view of the fact that physical progress has to be in relation to activities programmes and schemes, while the progress of expenditure has hitherto been reported or exhibited in terms of objects such as pay of officers, pay of establishment, contingencies, etc. An important requirement of planned economic development is a system of data reporting that would establish a rapport between the financial and physical aspects. In our view, the reporting system should be increasingly oriented to meeting the needs and requirements of performance budgeting. Even though performance budgeting will, under our recommendations, cover a limited area of the entire Governmental activities in the initial stages, it will, we envisage, be extended over a wider area in due course. In a matter like financial reporting, it is desirable that modern techniques should be adopted over as wide an area as possible. We are recommending elsewhere increased financial responsibility and authority to administrative Ministries and Departments subject to the pre-budget scrutiny of the Finance Ministry. Under the new set-up in which Departments would be responsible for their own financial management, there would be greater need of adequate internal reports for the use of both the Department and the Finance Ministry.

10.5 As regards the watching of the progress of expenditure, the Accountants General are required to intimate to the Ministries concerned the approximate figures of expenditure by major heads by the 10th of the succeeding month and of figures of expenditure under minor heads and primary units by the end of the succeeding month after the monthly accounts are closed. There are complaints, however, that the expenditure statements are not always received regularly. We express the hope that the Comptroller and Auditor General and the administrative Ministries will in consultation with each other take steps to ensure that the figures are submitted punctually at all levels of the organisations.

10.6 As regards the post-budget control to be exercised by the Finance Ministry, it is essential for the proper discharge of their functions that they receive the prescribed reports in time and regularly. In actual practice, however, certain Ministries have, we understand, been rather remiss in sending the half-yearly statements of the staff strength. The copies of the sanction orders issued under the delegated powers are not, for instance, received regularly in the Finance Ministry. The form prescribed for sending half-yearly reports has been recently amplified in certain aspects. It should, in our view, be further amplified to incorporate information on some important points, for example, (i) the existing budget provision, (ii) the savings which have been located for covering the expenditure involved, and (iii) the issue numbers of the sanction orders.

10.7 As mentioned in more detail in Chapter XI of this Report, our proposals envisage certain limitations being placed on the powers of administrative Ministries to create posts and they assign a more positive role to the Finance Ministry in the matter of ensuring that the expenditure on staff and establishment is more strictly scrutinised and kept under control. In view of this, it is all the more important to ensure that the half-yearly statements of the administrative Ministries are more informative and are submitted punctually.

10.8 We have referred to the difficulties experienced by the administrative Ministries in watching the progress of expenditure and have also suggested what steps should in our opinion, be taken to remove the difficulties. The real solution, in our view, would lie in transferring the responsibility for the maintenance of accounts to the administrative Ministries or Departments concerned. The departmentalisation of accounts and the delegation of financial powers to the administrative Ministries are two facets of the same process of transferring the entire responsibility of financial management and administration to the administrative Ministries. The question of accounting reforms is being examined by another Study Team. What we wish to do here is to emphasise the need for strengthening the accounting arrangements in such a way that the Ministries, and the other administrative authorities below them, can discharge their respective responsibilities in as full, unhampered and effective a manner as possible.

PART
TWO

EXPENDITURE CONTROL



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CHAPTER XI

DELEGATION OF FINANCIAL POWERS.

11.1 The existing rules provide that, subject to general or special orders made by the Ministry of Finance, no Department shall without the previous concurrence of the Ministry of Finance, issue any orders which may -

- (a) involve any abandonment of revenue or involve any expenditure for which no provision has been made in Appropriation Act;
- (b) involve any grant of land or assignment of revenue or concession, grant lease or licence of mineral or forests right or a right to water, power, or any easment or privilege in respect of such concession;
- (c) relate to the number of grades of posts or to the strength of a Service or to the pay or allowances of Government servants or to any other conditions of their service having financial implications, or
- (d) otherwise have a financial bearing whether involving expenditure or not.

There are identical provisions in the Rules of Business of State Governments. It may be added that the inclusion of a particular provision in the budget does not by itself confer authority to spend it. All this can be, and in practice often is, unduly restrictive. That financial control is needed goes without saying; that this control vis-a-vis the administrative structure, should ultimately vest in the Finance Ministry, may also

be accepted. But it will be noticed that while the rule lays down a general restriction, it also incorporates an important proviso. Far from being absolute, the restriction is subject to such general or special orders as may be made by the Finance Ministry. Control and delegation go together and what the rule envisages is not only financial control but also, and more importantly, financial delegation. The content of this delegation has been increasing from year to year. Various committees and authorities have, over the past twenty years, expressed views on the adequacy or otherwise of the delegations and recommended various measures. The views expressed and the action taken are summarised in Annexure 'A' at the end of this chapter..

11.2 It was for the first time under a scheme introduced in 1958 that a substantial delegation of financial powers was made to the administrative Ministries. The main features of this scheme were as follows :-

- (i) The power of the administrative Ministries to create temporary posts upto a period of two years was enhanced to include posts upto a pay scale going up to Rs.2250/- p.m. Permanent posts could be created in Classes II, III and IV.
- (ii) Subject to the existence of budget provision, administrative Ministries were authorised to issue expenditure sanctions on any scheme the total expenditure of which did not exceed Rs. 50 lakhs.
- (iii) The administrative Ministries were delegated full powers without any monetary ceilings, in respect of grants-in-aid and loans where schemes and pattern of grants and loans had already been approved by the Ministry of Finance.

- (iv) Full power to place contracts and to make purchases was delegated with a ceiling of Rs. 25 lakhs. In the case of single tender contracts the value was Rs. 10 lakhs and in the case of proprietary stores the ceiling was Rs. 5 lakhs. In the case of the Ministry of Works & Housing, the monetary limit was Rs. 50 lakhs in the case of single tender contracts and Rs. 1 crore in other contracts.

11.3 The twin aspects of control and delegation continued to engage the attention of Government. In 1961, for example, a further scheme of delegation was worked out and included in a paper on 'Measures for strengthening of Administration' laid by the Prime Minister on the Table of the Lok Sabha. The paper said :

"Responsibility for financial management should be devolved in greater measure than before both on the Ministries and executive agencies. The scheme now approved includes (a) formulation of programmes for intensive pre-budget scrutiny between the Ministry of Finance and administrative Ministry necessitating the preparation of budget estimates earlier than usual and (b) further liberalisation of financial powers to the Ministries in order to avoid references to Finance Ministry in the post-budget period except in vital matters and (c) the exercise of control of important financial aspects by the Finance Ministry through adequate reporting system and test checks."

11.4 As a result of the review of the earlier reforms and a better realisation of the problems that confronted the execution of the Five-Year Plans, a scheme based on devolution of a greater measure of financial responsibilities to administrative Ministries was introduced in September, 1961, on an experimental basis, in the four Ministries of Commerce and Industry, Community Development, Panchayat Raj and Co-operation, Information and

Broadcasting and the Department of Food. This scheme envisaged the exercise of control by the Finance Ministry mainly through pre-budget scrutiny and through random checks and work studies. The scheme was extended to other Ministries and departments of the Government of India with effect from 1st June, 1962. The main features of the scheme are given in Annexure 'B' at the end of this chapter.

11.5 On account of the emergency arising in the wake of the Chinese aggression towards the end of 1962, the scope of the delegation made in the circular of June 1, 1962, had to be modified in certain respects the most important of which were (a) posts (other than those required for security and Plan purposes) could be created only with the concurrence of the Ministry of Home Affairs and the Ministry of Finance, and (b) proposals for new constructions could be sanctioned only with the concurrence of the Ministry of Finance, even though covered by the existing budget allotments.

11.6 The position was reviewed towards the end of 1965 and orders issued in March, 1966, reintroducing the scheme of delegation as it had obtained in June, 1962. The effect of the orders is that the Ministries have full authority to spend within their budget provision; they exercise this authority in consultation with the internal Financial Advisers, but have no need to seek the sanction of the Finance Ministry. Moreover, the Ministries have been given full powers to sanction expenditure on the

various constituent schemes included in a project irrespective of the magnitude of the expenditure involved, provided that the project as a whole has been scrutinised and accepted by the Ministry of Finance. They have also been given powers to sanction, in their discretion, excess expenditure over the original estimates of the sanctioned schemes upto 10% or Rs. 1 crore whichever is less in cases where the administrative Ministry is satisfied about the special circumstances justifying the excess. As a result of this review, fresh instructions on the subject were issued in the Ministry of Finance O.M.No. F.10(50)-E(Coord)/65 dated 15th March, 1966.

11.7 An important feature of the present system of delegation is that, theoretically, the scrutiny by the Finance Ministry is mainly pre-budget. Once that stage is passed the Ministries have large powers to incur expenditure, enter into contracts, and generally proceed with execution. This should work extremely well if one important condition was satisfied, namely, that the Finance Ministry did in fact scrutinise most schemes at the pre-budget stage. Unfortunately, there remains a large proportion of cases in which the condition is not fulfilled.

11.8 It is clear that many steps have to be taken by the authority in charge of the execution of a major project before the project itself is worked out to the last detail. A scheme of delegation which does

not become operative until the last detail is approved by the Finance Ministry is, therefore, not very satisfactory. More than one instance has been brought to our notice of such postponement of delegation in respect of major projects. We are of the view that, once the preliminary feasibility report has been prepared and is accepted by Government, the administrative Ministries should be permitted to sanction expenditure on essential preliminary items upto a certain limit of their estimated cost.

11.9 Even where no detailed project report is involved, delay sometimes occurs in the process of scrutiny and examination by Finance. We suggest the setting of a time limit, say, four to five months, within which the approval of the Finance Ministry to the project or schemes should be accorded; failing which there should be a provision for the matter being automatically brought for decision before a Committee presided over by Cabinet Secretary.

11.10 One of the powers delegated to Ministries is that of reappropriation within each of certain specified groups of schemes, the grouping itself in each case being approved by the Finance Ministry. This approval is lacking in many cases and the power therefore is largely unexercised. It may be that the administrative ministries themselves have not in many instances approached the Finance Ministry with specific proposals for the grouping together of allied schemes. The matter, however, should

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not be allowed to rest there. Delegation is not the perquisite of a Department but, a requisite of the system. It would be only appropriate, therefore for the Finance Ministry to play a more positive role in this context and obtain from the Ministries, for purposes of approval, lists of related schemes at the time of formulation of budget.

11.11 The existing powers of reappropriation of the Ministries are specified in certain rules made in 1958. These have been modified from time to time. Even so, there are lacunae which need to be filled and we suggest a review of these rules for the purpose of vesting more such powers in the administrative Ministries. Further we are of the view that the delegation of other powers to Ministries - e.g., in the matter of negotiating contracts and placing orders for materials and supplies - are unduly restrictive in various respects. We suggest that in this instance as well the existing provisions should be reviewed and revised with the object of enhancing the powers of the administrative Ministries concerned.

11.12 While generally we have suggested greater financial delegation, there is one matter in which we recognize the need for greater overall control : the creation of posts and the resultant increase in establishment costs. Subject to the availability of funds and the location of savings, the Ministries are now competent to create

temporary and permanent posts on any approved scale of pay, etc. The opinion has been expressed both in Parliament and elsewhere that there is considerable overstaffing in Government departments and demands have been made from time to time for reduction in the expenditure on staff and establishment. It has also been felt, ~~that~~ under the delegated powers, the Ministries have been prone to create posts more liberally and with less rigid application of the standards or norms for the creation of such posts with the result that there has been avoidable expansion of staff. It is true that under the existing arrangements, the Ministries are required to consult the Work Study Units before creating new posts. Where separate work study units do not exist, this function is entrusted to the O & M Units. Many of the Work Study Units have not built up the expertise required for their being effective advisers in this respect of the Ministries of which they are a part. We are of the view that this function should be entrusted to a more specialised agency, detached from the day-to-day work of the particular Ministries which are advised.

11.13 We are further of the view that proposals for additional staff or creation of posts should be considered by a well-trained staff inspection unit composed of officers with adequate training in methods of work study, work measurement, etc. While the present

Staff Inspection Unit, in the Ministry of Finance may serve as a nucleus, with certain adjustments in composition, we consider that the new unit proposed should be located, not in the Finance Ministry, but in the Ministry of Home Affairs or in the Cabinet Secretariat.

11.14 The limitations on the powers of administrative Ministries to create posts which we have suggested above may, however, create difficulties, for example, in the case of a sudden increase in work or on account of certain work of an emergent nature devolving on a Ministry and in such circumstances it would obviously be necessary that they should continue to have powers to create posts of a purely temporary nature to cope with such a rush of work. We would, therefore suggest that in such cases of urgency the Ministries should have powers to create, during the course of a financial year for very short periods not exceeding three months in all, temporary posts in Class II, III and IV if funds to meet the cost of these posts can be found by valid reappropriation within their budget provision. This will also apply mutatis mutandis to the relevant departments and heads of departments.

11.15 In the light of the limitations which we have suggested on the powers of the administrative Ministries to create posts, it will be necessary also to restrict powers of reappropriation in one respect. In this case what we would recommend amounts to the revival

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of an older restriction. This precluded Ministries from augmenting the provisions under the "Pay of Officers" and "Pay of Establishment" by recourse to reappropriation. This rule might be revived with the slight modification that when purely temporary posts are created in exercise of the Ministries' own delegated powers in the manner indicated above, the additional funds for such posts could be found by reappropriation. In all other cases of creation of staff the Ministries will have to go through the normal channels for obtaining funds. This will enable more effective scrutiny of proposals for augmentation of staff.

11.16 We have one other suggestion to make regarding powers of reappropriation. The present position is that a sum provided under the head 'Plan' in a Demand for Grants is available for plan schemes only; in other words savings in plan expenditure cannot be diverted for non-plan purposes by the Ministries without the specific prior concurrence of the Finance Ministry. This restriction serves a purpose, but the converse should certainly be permitted. A provision made under the head 'Non-Plan' for a scheme and not utilised should be allowed to be reappropriated for a plan scheme under the delegated powers of the Ministries without their having to come to the Finance Ministry.

ANNEXURE 'A'

Summary of the views on delegation
of financial powers given by various
authorities and action taken prior to 1958.

A. Summary of views.

<u>Name of the person/ committee</u>	<u>Year</u>	<u>Summary of comments</u>
1. Sir James Grigg.	1934-39	The system of detailed sanction involved a good deal of wastage of time and efforts at both ends; it also made a timid attitude on the part of administrative departments.
2. Sir Richard Tottenham.	Nov. 1945	The existing system of day to day control by the Finance Department tended to blunt the financial conscience of the spending Departments, and that better results, combined with a great decrease of work could be obtained by putting financial responsibility more squarely on the latter. He also wanted "Contract Budget" or Commitments budget to be introduced.
3. Shri Gopala- swamy Ayyangar.	1949	The Ministry of Finance is unwieldy there is far too much centralisation it concerns itself not merely with the general financial policy of the government or the main heads of public expenditure but also with every detail in the administrative execution of proposals for which the need has been accepted by Government as well as the legislature. The problem is to bring about such changes in machinery and procedure as would render the processes of expenditure sanction more intelligent, well-informed and speedy and thereby remove the sense of frustration which afflicts several Ministries and Departments. A compendium/guide of financial rules should be issued.

4. Estimates Committee
First Lok Sabha
Second Report.

1950-51

"In order to avoid unnecessary delay in the day to day performance of the normal functions of a Ministry, greater financial powers in the field of minor items of expenditure should be devolved on the heads of Ministries and Departments."
5. Shri A.D. Gorwala.

1951

There are many bitter complaints relating to woodenness and lack of discrimination of the Finance Ministry at the Centre. It centralises in itself the power of sanction, and even for small amounts of expenditure the Administrative Departments have to go to the Finance Ministry.

In the States the relations between the Finance Department and other Departments are much more cordial.
6. Dr. Paul H. Appleby.

1953

There is an astonishing lack of capacity and/or facilities for administrative delegation. The financial control was too much in the hands of persons remote from action and programme realities.
7. Shri C.D. Deshmukh.

1953-54

The general procedure followed was sound but there was a need to avoid reference of trivial matters to the Ministry of Finance.
8. Estimates Committee
Report
(9th Report)

1953-54

The delegation of financial powers had become a necessity in view of the changed circumstances. After the scheme has obtained Financial concurrence from the Ministry of Finance, the detailed execution of the scheme and spending of money thereon should be the responsibility of the administrative Ministry concerned.
9. Shri A.K. Chanda.

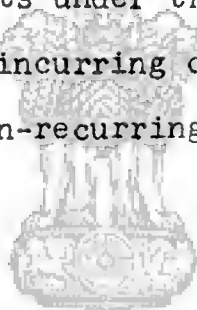
1954

The existing system of financial control is wasteful because schemes are, at present, drawn up without sufficient technical/financial advice. The present external financial advisers are not familiar with difficulties.

B. Action taken prior to 1958.

In May 1955 orders were issued enhancing the existing financial and cognate powers to the administrative Ministries and Heads of Departments, as the powers enjoyed by them prior to this were extremely limited, for example, the Ministries had hitherto powers to create posts only in Class III and IV for their own offices. As a result of the delegations made in May 1955, the Ministries were given powers to create Class I and Class II posts not above the rank of Under Secretary up to two years in their own establishment as well as under other establishments under their control.

Similarly the powers of incurring contingent expenditure of both recurring and non-recurring nature were enhanced.



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ANNEXURE 'B'

Main features of the Scheme
of delegations in 1962.

1. A proper scrutiny of the schemes, etc., submitted by the administrative Ministries for incorporation in the Budget should be carried out by the Ministry of Finance before including such proposals in the Budget. It has, therefore, been decided that budget proposals should be prepared by Ministries in greater detail and with as much precision as possible and referred to Finance Ministry a few months earlier than usual, say from the beginning of July each year.
2. Arrangements have been made with the Accountants General for the regular and timely supply of accounting data to the administrative Ministries to enable to steady expenditure against the appropriations.
3. Lump provision can be made for urgent schemes not yet ready in detail. But sanction against such provision can be issued only after the scheme had been accepted by the Ministry of Finance.
4. This scheme of delegation of powers also provides that any amounts, without specified limits, may be sanctioned by the administrative ministries if the projects for which such amounts are sanctioned, have been earlier scrutinised and accepted by the Ministry of Finance. It may be noted that under the powers delegated in 1958, the administrative Ministries were authorised to sanction expenditure upto Rs.50 lakhs only.
5. The administrative Ministries have been delegated powers to incur expenditure on all items irrespective of the fact whether these are new items or otherwise, so long as such new items form part of an approved project.
6. The Administrative Ministries have also been delegated full powers for reappropriation between the primary units. To facilitate the exercise of these powers,

it has been provided that the primary units consisting of allied schemes be formed into groups and such groupings be got approved by the Ministry of Finance.

7. The administrative Ministries have been authorised to create posts upto a pay scale of Rs.3000/- p.m.
8. Powers have also been delegated to the administrative Ministries to sanction excess expenditure over the original estimates upto a limit of 10% or Rs.1 crore, whichever is less, in cases where the administrative Ministry is satisfied about the special circumstances justifying the excess.
9. It has been made an integral part of the scheme of 1962 that each Ministry should set up, internally, a competent work study unit which would assist the Ministry in laying down norms for particular types of work and would also examine such proposals for staff re-organisation or creation of posts (both in the Department and in offices under it) as are referred to it.



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CHAPTER XII

ROLE OF FINANCIAL ADVISER

12.1 It is unnecessary for our purposes to trace the successive changes which have taken place in the role and functions of the Financial Adviser. A distinction has to be drawn between:-

- (a) the External Financial Adviser whose main function is to exercise some of the powers of the Finance Ministry and advise on its behalf; and
- (b) the Internal Financial Adviser whose main function is to assist in the exercise of powers delegated to the Administrative Ministry.

This description may be amplified in order that the issues may become clear:

(i) The External Financial Adviser has obviously, in that capacity, to be responsible to the Finance Ministry. But while discharging various functions on behalf of that Ministry there is nothing to prevent his being asked to advise in the delegated sphere as well. In one sense, this would be a combination of the roles of External and Internal Financial Adviser.

(ii) An Internal Financial Adviser strictly so called - i.e. one who does not exercise any powers whatever on behalf of the Finance Ministry - will nevertheless obviously concern himself not only with financial matters finally disposed of by his own Ministry, but also with those which -

being outside the delegated sphere - necessitate a reference to the Finance Ministry. This, however, is not a "combination" of roles as in (i) above.

(iii) One distinguishing feature of internal financial advice is that it must be susceptible of being overruled within the Ministry itself. The level at which it may be overruled, and the conditions (if any) subject to which it may be overruled are points of relative detail, though important in themselves. (If, for example, it is laid down that, every time such advice is overruled, one or more of various authorities - e.g. Finance Ministry and Auditor General - should be notified, this would be a significant restriction on the exercise of the relevant powers of the Administrative Ministry.)

12.2 The latest position may be summarised as follows: Certain financial powers are delegated to the Administrative Ministries. In the exercise of such powers it is open to the Ministry--(a) whether or not to make purely internal arrangements for financial advice; (b) in the event of making such arrangements, whether or not they should take the form of appointing an Internal Financial Adviser, strictly so called and (c) in the event of not appointing an Internal Financial Adviser, whether or not to refer one or more categories of cases (within the delegated sphere), for advice, to the Finance Ministry, it being understood that such advice is not binding on the Administrative Ministry.

12.3 We may now consider certain views relevant to the role and functions of the Financial Adviser. The proposition is advanced, on the one hand, that the advice from a person subordinate to the Secretary of a Ministry is not likely to be independent and objective and is bound to reflect the situation under which the Financial Adviser is directly subordinate to the Secretary of the Ministry on whose confidential report his preferment and future prospects would greatly depend. There is, on the other hand, the point of view that advice proceeding from a person within the Ministry will be more uninhibited and informed since he will be intimately associated with, and will have intimate knowledge of, the working of the Ministry and its organisations and projects. Here as elsewhere we consider the over-riding need to be that of prompt decision and speedy implementation. It is of vital importance, from this point of view, that the responsibility for execution should rest squarely on the Ministries and departments concerned. It is in the discharge of these responsibilities and as an integral part thereof that the need arises for internal financial advice.

12.4 We are, therefore, of the view that the Secretary of a Ministry should not only be delegated all the necessary powers, but, in their exercise, be assisted by a competent Finance Branch or Section under

him. His own responsibility should remain unimpaired, and he should therefore have the power to overrule the Financial Adviser, where necessary. Since the delegated powers that we envisage will be quite large, references outside the delegated sphere will be much fewer than at present and can be conveniently addressed direct to the Finance Ministry. We, therefore, see no place for an External Financial Adviser in the arrangements we contemplate. The Financial Adviser of our recommendations will be a purely Internal Financial Adviser with no functions to discharge or responsibilities to exercise on behalf of the Finance Ministry. He will be responsible to, and under the administrative control of, the Secretary of the Administrative Ministry. So long as this is clearly understood, however, we see definite advantages in the Financial Adviser being appointed with the concurrence of the Finance Ministry. The annual assessment of his work, like that of other officers of the Ministry should be recorded by Secretary of the Administrative Ministry. We would suggest, however, that in order to ensure greater objectivity and better assessment of the professional and technical aspects of his work, the report of the Secretary, Expenditure Department should also be obtained and incorporated in the annual confidential report. We envisage, on the part of the Finance Ministry, an overall and co-ordinating interest in the careers of Financial Advisers.

12.5 The Financial Adviser that we contemplate will be a senior officer with adequate background and training. Like his counterpart in the United Kingdom, he will be among the most important officers of the Ministry. He will assist and advise the Secretary in the exercise of the financial powers of the Ministry and will be entitled and expected to put forward his views on all financial matters before decisions are reached. He will organise financial management and control in all matters within the Ministry's field of responsibility and maintain the requisite liaison with the Ministry of Finance. He will be placed in charge of the Finance and Budget Cells of the Ministry. It will be open to the Secretary of the Ministry to overrule him without having to report the fact to any one, but there is another and more positive side to the relationship between the Secretary and the Financial Adviser, namely that the former will attach the highest importance and give the most careful consideration to the views expressed by the Financial Adviser. The relationship between them should be that of senior partners in a common enterprise.

12.6 We would make certain detailed observations regarding the scheme of financial advice as it now obtains (Memorandum of March 15, 1966):-

- (1) The first point is with regard to the procedure of consultation with the Financial

Adviser. It is provided that a Ministry would lay down in its discretion the procedure for consultation with the Financial Adviser. It would be of advantage, in our view, to provide for the formulation of a uniform set of rules, for the guidance of Administrative Ministries.

- (ii) Secondly, at present it is within the discretion of the administrative Ministries to decide whether or not a whole-time Financial Adviser is needed. It is imperative as mentioned earlier that the Administrative Ministries should, in the exercise of their powers over a vast delegated field, have the benefit of proper financial advice. This should, in our view, be provided by a well-organised system and through a mechanism by which the financial aspects of a proposal or the financial considerations that should weigh in decision-making should regularly and systematically be presented to them. It should, therefore, be obligatory on each Administrative Ministry to have an Internal Financial Adviser though on considerations of work load etc. it should be open to Government to entrust to one official the work relating to more than one Ministry.

- (iii) The third point requiring attention is the financial organisation within the Administrative Ministries. The orders of 1962 (No. F.10(4)-E/(Coord)/62 dated 1st June 1962) clearly

envisaged the Ministries organising their Finance, Budget, and Accounts cells suitably to implement the new scheme of delegation of powers. It is necessary that the Finance Branches of the administrative Ministries should be strengthened where necessary, and staffed with trained and qualified personnel. The Ministry of Finance have also a responsibility in the matter. They should, we would suggest, help the Administrative Ministries to organise well-equipped internal finance branches manned with qualified and well-trained personnel. It will be necessary (a) to ensure proper training of the junior ranks, (b) to provide, for the middle ranks, varied experiences and knowledge of the different fields of public administration and (c) to devise a careful system of selection and inter-change between departments in respect of the higher echelons. A fresh assessment of the requirements of the Finance Branches may also have to be made in the light of the requirements of performance budgeting, about which we have made our recommendations earlier in this Report.

- (iv) Lastly, it should be made perfectly clear by Government that it is no longer necessary

for an administrative Ministry to refer for decision to the Finance Ministry (other than a point of interpretation or clarification) any matter which is within the delegated field. In all such cases, the Administrative Ministry should exercise responsibility on its own. Conversely, the Finance Ministry should refuse to entertain references falling within the delegated sphere of an Administrative Ministry.

12.7 It will be necessary to mention, however, that under this scheme of Internal Financial Advisers some increase in staff would be involved, at any rate in the initial stages. The number of Financial Advisers would have to be increased since an Internal Financial Adviser, by the very nature of his duties, has to be an integral part of the Ministry and cannot adequately and effectively discharge his duties if (except when the Ministries or Departments are relatively small) he is called upon simultaneously to act in that capacity to a large number of them. The process of strengthening the Finance and Accounts branches of the departments may also involve some expenditure. But having given weight to the considerations of speed in decision-making and execution and to the need of improved financial management systems and practices, we cannot help feeling that this additional expenditure would be well worth incurring, since it would be repaid by a better and more efficient financial management.

12.8 Apart from the personal qualities so very requisite for these posts, it is necessary that Financial Advisers should have a background of administrative experience. It is also necessary that they should at an appropriate stage be given adequate orientation in relation to the duties of Financial Adviser.

12.9 Finally, we support the principle of periodical interchange between the Financial Wing and other branches of administration. This will not only enrich the experience of those who are thus interchanged but also, in the long run, make for sounder finance as well as sounder administration.



मन्त्रमिव ज्ञायते

CHAPTER XIII

CONTROL BY PARLIAMENT

13.1 In discussing the budget - which is the authority for all Government spending - and in voting the budget grants, the Legislature is in fact exercising a basic form of expenditure control. The control continues in another form after the budget is passed. The object is to ensure that the funds appropriated by the Parliament have been utilised for the purposes specified and in the manner intended. In this phase of parliamentary control, the instruments are the Financial Committees of Parliament, namely, the Public Accounts Committee, the Estimates Committee and the Committee on Public Undertakings. In this Chapter we discuss the role of these Committees and their possible re-orientation in the light of new requirements.

13.2 The Public Accounts Committee is the most important of the Parliamentary Committees on public expenditure. This Committee was constituted at the Centre and in the States on the inauguration in 1921 of the Montague-Chelmsford Reforms and has been continuously in existence since then. As now constituted, the Committee consists of 15 members elected from the Lok Sabha and seven members from the Rajya Sabha.

13.3 The main functions of the Committee are to ensure (a) that the moneys shown in the accounts as having been disbursed were legally available for and applicable to the service or purpose to which they have been applied or charged; (b) that the expenditure conforms to the authority which governs it; and (c) that every reappropriation has been made in accordance with the provisions made in this behalf under rules framed by competent authority.

13.4 Though essentially concerned with the aspects of appropriation, the scope of the Committee's actual work extends to aspects such as prudence, economy and financial propriety. The Committee's reports have been instrumental in giving considerable publicity to individual instance of departure from sound standards of public expenditure.

13.5 The functions of the Estimates Committee are different from those of the Public Accounts Committee. The Estimates Committee was constituted in 1950 and consisted originally of 25 members, but the strength was raised to 30 in 1955. The members are drawn exclusively from the Lok Sabha and their term of office is one year.

13.6 The functions of the Estimates Committee are as follows:-

- (a) to report what economies, improvements in organisation, efficiency or administrative reform, consistent with the policy underlying the estimates, may be effected;

- (b) to suggest alternative policies in order to bring about efficiency and economy in administration;
- (c) to examine whether the money is well laid out within the limits of the policy implied in the estimates; and
- (d) to suggest the form in which the estimates shall be presented to Parliament.

Though the Committee is known as an Estimates Committee, it does not examine the Budget Estimates presented to the Parliament. It is concerned with 'estimates' only after they have been presented to the House, and it takes up for examination the various current activities reflected in these estimates. The main objectives of the Committee are to secure economy and efficiency in administration, and to ensure that money is well laid out, but if a closer examination reveals that a certain policy is defective or that its implementation involves wastage of funds, the Committee may with supporting reasons, suggest an alternative policy for the consideration of Parliament.

13.7 The control exercised by the Estimates Committee is not direct but is felt mainly by virtue of its influence on the decisions of the Government. One of the limitations of the working of the Committee is, however, the time lag between one review and another of the same department. This is because the Committee can concentrate at any one time on only one or two Departments and it naturally takes a long time before it can come back to the same Department. Moreover, the Committee does not have the benefit of such competent technical advice as the Public Accounts Committee has from the Comptroller and

Auditor General.

13.8 The third Committee of the House is the Committee on Public Undertakings consisting of 15 members: 10 elected by the Lok Sabha and 5 elected by the Rajya Sabha from among their Members. This Committee is a relatively recent creation; it started functioning in 1964. The scope of the Committee's work is (a) to examine the reports and accounts of public undertakings; (ii) to examine the report, if any, of the Comptroller and Auditor General of the public undertakings; (iii) to examine in the context of autonomy and efficiency if the public undertakings are being managed in accordance with sound business principles and prudent commercial practices and (iv) to discharge such other functions vested in the Public Accounts Committee and the Estimates Committee in relation to the public undertakings, as are not covered under items (i), (ii) and (iii) above and as may be assigned to the Committee by the Speaker from time to time. The Committee undertakes its studies of individual public undertakings, by rotation.

13.9 The question is sometimes raised whether there is not a certain amount of duplication in the functions and responsibilities of these Parliamentary Committees and whether it is really necessary to have three Committees doing work of almost similar nature. In particular, there is considerable overlapping between the spheres of activities of the Public Accounts Committee and the

Estimates Committee and then again between those of the Estimates Committee and the Committee on Public Undertakings. It has already been noticed that the task of the Estimates Committee is not, as in the case of the Standing Finance Committee, to exercise a pre-budget scrutiny of the items of expenditure but only to examine the estimates after they have been presented and approved by the Parliament. The need of having a Parliamentary Committee for this limited purpose is questioned by many.

13.10 In considering the re-orientation and in some aspects the reorganisation and rationalisation of these Committees, we believe that certain points should be borne in mind. We formulate them below partly in the shape of observations and partly as recommendations:-

- (i) Parliament's time is valuable. In so far as the Committees draw Parliament's attention to specific matters, these matters must be so important as to justify Parliament devoting time and attention to them.
- (ii) In the context of parliamentary control the matters in question may be classified as:
 - (a) accounts:

the proper spending of moneys sanctioned by Parliament; and
 - (b) performance:

the effective implementation of programmes approved by Parliament.

It may be remarked in passing that (a) and (b) are only two sides - (a) in terms of cash and (b) in terms of results - of the same transactions.

(iii) It follows from (i) that both in regard to proper spending (accounts) and effective implementation (performance) only the most important items should be brought to the notice of Parliament.

(iv) So far as proper spending is concerned, the Public Accounts Committee is the appropriate instrument of control; it should however confine its attention, and therefore its comments, to items of outstanding importance; and since the items dealt with by it are those included by the Comptroller and Auditor General in his Appropriation Accounts and Audit Report, it follows that the Comptroller and Auditor General for his part should ensure that this document deals only with the most important items.

(v) If the suggestion in (iv) is carried out, it automatically follows that the Public Accounts Committee will confine itself to functions which are both important and constructive. It will not deal with minor matters, including relatively small irregularities, in such a manner as to lay itself open to the criticism that it is

helping to hinder initiative. It will, of course, continue to comment upon and draw pointed attention to instances of major irregularities. But, by the same token, too much of its time - and therefore of Parliament's - will not be spent on the bona fide decision of those in positions of executive responsibility. Nothing is easier to inculcate than the habit of not taking decisions. And those hitherto accustomed to take decisions - and therefore risk - might hereafter desist from doing so if the only result, in the event of something going wrong, is adverse notice by the Public Accounts Committee and a blaze of unenviable publicity in Parliament.

- (vi) If the Public Accounts Committee is thus enabled to confine itself to a relatively few important items, there is no reason why it should not also deal with the expenditure side of public undertakings.
- (vii) The aspect that remains to be dealt with is Performance, viz., programmes, actions and results not only of Departments but also of public undertakings. This could well come under the purview of one Committee specially constituted for the purpose and the present duplication of functions (as between the Estimates Committee and the Public Undertakings

Committee) avoided.

- (viii) In order that the performance aspect - no less than the accounts aspect - is properly examined, analysed and presented to Parliament, it is necessary that there should be some organisation or group of experts to review and evaluate results, cost, efficiency and other aspects of performance. This organisation might grow pari passu with performance budgeting as a feature of the Central budget and the State budgets.

13.11 We may now proceed to work out the practical application of these considerations. We consider that the influence of the Committees of Parliament would be considerably enhanced if reorganisation is effected in the manner indicated above. In regard to the Public Accounts Committee, we would suggest that the Committee should, as has indeed been generally the case in the past, refrain from taking cognisance of matters involving administrative decisions or policy formulations unless these have been specifically reported to Parliament by the Comptroller and Auditor General in his audit report or in the appropriation accounts. To do otherwise would be an unhealthy departure from the practices and conventions which have stood the test of time. It is obviously important that this Committee, with its great potentialities for good, should exert pressure on points where it can bestow the greatest benefit and that it concentrate its attention on major

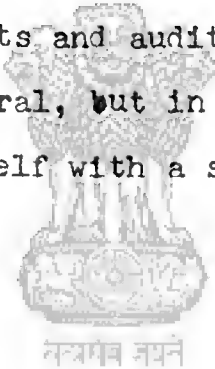
matters of major importance. We have suggested that the jurisdiction of this Committee should be enlarged so as once more to include the expenditure side of public undertakings.

As regards the other two Committees - the Estimates Committee and the Committee on Public Undertakings - our proposals are indicated in the following two paragraphs.

13.12 We have at different places in this report laid considerable stress on the performance aspect both of budgeting and review. The last-mentioned function, namely, review of performance in relation to budgeted programmes is best done by a single committee of Parliament, which might be called the Performance Committee (corresponding to the Public Accounts Committee in relation to expenditure). The Performance Committee would then replace both the Estimates Committee and the Committee on Public Undertakings. The Performance Committee could have two wings, one dealing with the performance of the Government departments and Ministries and the other with the performance of the public sector undertakings. The Committee could be assisted by an organisation or a group of experts. These would assist the Committee in the same way as the Public Accounts Committee is assisted by the Comptroller and Auditor General. This Committee would place before Parliament a review of the progress of important projects, under the purview of

departments or statutory corporations or Government companies. It would also be concerned with the cost and efficiency aspects of the projects and therefore, in particular, be interested in a study and examination of the actual planning, cost - benefit analysis, and the physical achievements of these projects.

13.13 We recommend, therefore, that in place of the Estimates Committee and the Committee on Public Undertakings, there should be a single Committee with the designation of Performance Committee of Parliament. The Public Accounts Committee would continue to operate on the appropriation accounts and audit report of the Comptroller and Auditor General, but in the new set up it would, in addition, concern itself with a similar report on public undertakings.



CHAPTER XIV
CHANGES IN PERSPECTIVE

14.1 We would preface our concrete suggestions in this and the following chapters by certain general observations on the substance of the financial relationship between the Centre and the States. This is because the procedural aspects with which, in a literal sense, we are concerned cannot be considered in isolation from institutional aspects, and the latter in turn are inseparable from the actual substance of the relationship as it undergoes change from time to time. Such change is inherent in any structure which is truly federal. It follows that in such a structure the relations between the Centre and the States cannot be readily codified. Institutions and procedures have to be adapted, not indeed frequently, but as occasion demands, to any substantial change of the political and economic context. Otherwise, procedures once considered appropriate might become sources of friction or frustration and seriously affect the operation of the federal relationship. Some of the important changes are enumerated in the following paragraphs.

14.2 When the federal Constitution was drawn up, it incorporated an important aim of federal finance, namely, the provision of certain basic services and opportunities to all the constituent units, having

regard to their varying stages of development. This principle was sought to be made effective by a periodical devolution of Central taxes and disbursement of Central assistance among the various States on the basis of suitable criteria and through the instrumentality of the Finance Commission. But the context changed with Planning. It was considered necessary that the Centre should play an effective role in the whole process of development. This new role, it was thought, would be best fulfilled by the establishment of the Planning Commission. Among the most important levers operated by the Planning Commission was assistance to the States for financing their Plans. The Commission, conjointly with the Ministries, determined the quantum of the loans and grants to be given to the States for specific purposes. It also devised formulae which laid down in detail the conditions on which the loans or grants became payable. This one development altered the whole profile of the Centre-State financial relations. The constitution contemplated most of the grants being provided under Article 275(1), the quantum and the basis being determined by the Finance Commission. This was, however, overshadowed by the new form of discretionary assistance from the Centre to the States under Article 282 of the Constitution, for the implementation of their Five-Year Plans. Thus the aggregate of Plan loans and grants (including those for Centrally sponsored schemes), expressed as a ratio

of the ~~total~~ 'own resources' of the States, has gone up from 24.8% in 1951-52 to 70% in 1965-66. In contrast, the corresponding ratios for statutory grants to States are 4.8% in 1951-52 and 5.6% in 1965-66. For the amounts transferred to States by the devolution of taxes and duties, the corresponding ratios are 14.9% in 1951-52 and 17.8% in 1965-66. It was thus the Planning Commission, rather than the Finance Commission, that began to play the major role in the allocation of resources to States (in the form of discretionary grants). This was hardly a position contemplated by the Constitution. It raised the question of what precisely were the role and functions of the Finance Commission.

14.3 Another important factor has been a growing demand on the part of the States that decision-making in regard to the Plan should be much more decentralised. A federal constitution implies that the constituent units have adequate freedom in their own sphere to evolve policies which are suited to their own circumstances. The demand for decentralisation has been fortified by recent political developments. This, then, is the changed political context.

14.4 The economic context of the planning process has also undergone significant changes in recent years. There has always been a tendency to emphasise the 'needs' aspects of the Plan rather than its 'resources'

aspects. The result is that size has tended to be out of proportion to resources. This in turn has fostered an element of unreality in the formulation and implementation of the plans at the State level. Since the 'needs' aspect of planning is over-emphasised, the State Governments are tempted to exaggerate their requirements and ask for increasing aid from the Centre. But the Centre can no longer aid as in the past. Resources are lower, prices higher and expenditure larger. Neither the Centre nor the States can afford to take the line that if plan size is taken care of, plan resources will take care of themselves. It is in this context that the Centre-State relations have to be refashioned so that the plans in general and the State plans in particular become more resource-oriented and a larger degree of flexibility is introduced in planning at the State levels.

14.5 It would be necessary to see whether the objectives of the various procedures in regard to Central assistance have been achieved at all or whether somewhat different objectives have to be set. One of the main objectives of Central assistance to States has been to ensure that the States implement effectively those schemes and projects which have a certain rationale in the overall context of the national economy. In other words, the pattern of assistance devised was designed to facilitate the use of Central funds in channels pre-determined in the Plan. When it was found

that these objectives were not achieved on account of lacunae in the procedures underlying the release of Central assistance, many reforms were introduced to simplify the procedures. Even then, the main objective of ensuring that the funds were used so as to achieve certain results has remained largely unfulfilled.

Instead what has been achieved is an artificial uniformity in the schemes and projects of different States. In many instances, the States persuaded themselves to take up projects, not because of their own needs and priorities, but because the Centre gave them assistance on the condition that the prescribed patterns were adopted.

14.6 What is necessary, therefore, is clearly defined objectives of Central assistance, and consequent changes in procedures. These objectives should be as follows:-

(a) Certain basic priorities, kept to a minimum in number, have to be accepted by the Centre and the States; (b) subject to the foregoing, there should be a broad pattern of priorities which different States might adapt to their individual requirements; (c) the procedures of assistance should be such that the States are left with every incentive to develop and tap their own resources; and (d) all resources, whatever their origin, should be employed with the maximum economy and efficiency.

14.7 We are of the considered view that if these objectives are to be fulfilled, it will be necessary to reduce considerably the proportion of the discretionary element in Central assistance. The unconditional or 'untied' element of assistance would then increase. It should also be possible, as we shall later indicate, that the States can be told beforehand with reasonable certainty of the size of the untied assistance which each of them will, over a period, be entitled to. This, together with the resources they are able to mobilise themselves should enable the States to plan more realistically their own schemes and projects in the manner best suited to their individual circumstances while remaining within the broad framework of the all-India Plan.

14.8 It is in the light of the changed circumstances and requirements outlined above that the question of devising appropriate institutional arrangements has to be settled. The organisational pattern should be such as to reconcile the regional needs and conditions in individual States with the broader priorities of the nation as a whole. For this to happen, the degree of Central control and co-ordination should be regulated by two factors: the need to maintain a national perspective and the need to promote local initiative.

14.9 It would appear that it is only in a qualified sense that we can think hereafter of one plan for the whole country and one plan for all the five years. Within

the broader framework of major objectives and major strategy, the Plan has hereafter to possess two characteristics (i) flexibility in terms of the States and (ii) adaptability in terms of changing economic conditions. One consequence of this, in the limited context of Centre-State financial relations, would in our view, be the desirability of reviewing the size of the untied assistance we have mentioned above, not every five years, but at more frequent intervals, say, once in two or three years. If, as we later recommend, the untied assistance is determined by means of a semi-judicial award, there could be one award of two years and another of three years following each other in rotation, any one Plan period being covered by two such awards.

14.10 In the next chapter we deal with the Finance Commission and set out our proposals for reorganising it.

CHAPTER XV
FINANCE COMMISSION

15.1 An important function of the Finance Commission is to recommend the manner in which the residuary budgetary needs of the States may be met after taking into account the statutory devolution of Central taxes. The underlying idea is that, the constituent units, with their varying degrees of progress should where necessary be assisted to attain a minimum level of development. In the light of this principle, the various Finance Commissions devised their own schemes for determining the quantum of statutory assistance to States. By and large, the emphasis has been on the need to meet the "budgetary gaps" of the States, interpreted in a rather narrow sense of the term. The first Finance Commission (1952), argued that the budgetary needs of the States should first be estimated by a detailed examination of the forecasts of revenues and expenditures submitted and then these should be reduced to a comparable basis by the exclusion of abnormal, unusual and non-recurring items of expenditure. Adjustment in these analyses should ^{be} made to take account of the extent of tax effort made by each State individually and also the measure of economy it had effected in administration. This would then help a broad judgement on the quantum of assistance that would be required. This general

approach was sought to be qualified by a proviso that the level of grants-in-aid should be made dependent also on the level of social services reached in a State and any special disabilities to which it is subject should entitle it "to a further moiety of assistance".

15.2 Planning as we have pointed out, changed the entire context. It became more and more difficult to assess the "budgetary gaps", since the budgets themselves increasingly reflected Plan expenditure. As already noticed, the bulk of the finance for State Plans was latterly found through Central assistance. This change in the Centre-State financial relationship influenced to some extent the thinking of the Finance Commissions. The Second Finance Commission (1957) recommended such assistance to the States as along with the promised Central grants would enable them to put through their plans. The Third Finance Commission (1961) recommended that "the total amount of grants-in-aid should be of an order which would enable the States, along with any surplus out of devolution, to cover 75 per cent of the revenue component of their Plans". But the recommendation was not accepted. When it came to the Fourth Finance Commission (1965), however, the dichotomy between non-Plan expenditure and Plan expenditure - however unreal from the point of view of a State's finances as a whole - became very evident. For reasons which it is not necessary to go into here, the Fourth Finance Commission confined itself to estimating

the "non-Plan revenue gaps" of States. It recommended that these gaps should be eliminated by Central assistance. The whole question of Plan expenditure and resources to meet such expenditure was left to be tackled by the Planning Commission.

15.3 It is clear to us that one body, and not two different ones, should take a view of both Plan and non-Plan expenditure on the one hand and of all available resources on the other in order to arrive at a proper pattern of allocation to the States. In regard to such allocation, we are further of the opinion that what is needed today is a shift of emphasis, to the maximum extent possible, from discretionary grants to semi-judicial allocations. For obvious reasons the Planning Commission's decisions regarding apportionment of resources to States - however objective this might be - would not be regarded by the States themselves in the same light as the quasi-judicial awards of the Finance Commission. The allocation has to be done by an independent authority. Our ~~addition~~ conclusion is that the Finance Commission suitably reorganised for this purpose, should be entrusted with the total task, viz. of having a view of both Plan and non-Plan expenditure, both Central and State, and making the requisite allocations to the States. Before proceeding to suggest the lines on which the Finance Commission should be reorganised, it is necessary to examine the present position

regarding Central assistance generally.

15.4 The total Central assistance that is given to States (other than specific assistance for non-Plan purposes) falls into four main categories. First, there are the "statutory" grants under the awards of the Finance Commissions. Second, there are the Plan grants and loans given to States on a matching basis. Third, there are the Plan grants and loan schemes which do not call for a matching contribution from the State Government. Fourth, there is the Plan assistance, largely by way of loans, provided for specific identifiable projects of a manufacturing type or infra-structural in character such as irrigation, transport, power generation, water works, etc. Of these, the first category of assistance is "untied" and automatic. The assistance under the second category is conditional, being limited to specific projects or categories of schemes; in practice, however, assistance of this type is available under broad heads of development so that the States can utilise it on various individual schemes according to their preference. Assistance of this type is partly in the shape of grants and partly of loans. The third category of assistance is strictly tied to specific schemes and is also on the basis of both grants and loans. In the last category which is largely in the nature of loans for infrastructural and manufacturing projects, there is very little of the element of grant. All except the "statutory" grants currently fall within the purview of the Planning Commission.

15.5 We propose to reclassify this assistance into three categories. First, there would be untied assistance. This would cover all assistance generally with the exception of the two categories specified below, viz., the second and the third. The second category would comprise assistance which is earmarked for a very small number of schemes of basic national importance. The third category would consist of assistance for financing projects in certain major fields of developments such as power, major irrigation, transport and industry. The bulk of the assistance, as we have said, would belong to the first category; it would be untied and, like the present statutory grants, automatic. It appears from the budget documents of the Central Government that the sum total of (a) statutory grants to States and (b) Plan assistance for agricultural and other programmes broadly equals the current account surplus of the Central Government, excluding grants. It is necessary that appropriate criteria (not conditions) for allocation of assistance of this type should be devised. It is this function that should be vested in the reorganised Finance Commission. This body should be a permanent one. It would, in addition to its present function of devolution of taxes, devise criteria for allocating untied plan assistance among the various States. A major portion of assistance may have to be given on criteria relatable to population, area and

relative backwardness and the remaining assistance on criteria relatable to the States' Plan on the one hand and, on the other, its performance in the agricultural sector or other specific areas of development, the emphasis thus being both on future tasks and past results.

15.6 Since some proportion of this assistance, though automatic and on a non-discretionary basis, will be related to the performance of the States in agriculture and other spheres, the Finance Commission will have to review the achievements of each state. It has also to set up or co-ordinate the requisite machinery for this purpose. Further, it would be desirable that the awards of the Commission are given at intervals which are neither too long nor too short. That is why we have suggested that two successive awards, one for two years and the other for three years, together coinciding with a particular Plan period, might be suitable.

15.7 The reorganised Finance Commission would, of course, devise criteria for disbursing Central assistance under the first category in the light of the strategy, priorities and resources availability as laid down in the Plan. While thus it would take full account of Plan investments and estimates, it would, of its own, assess the extent of the total available resources, as also the portion which, out of such resources, might be set aside for allocation to States. Since the Plan mainly relies on estimates for the five-year period, the Commission would

be in a more advantageous position to revise and modify these estimates, if necessary, on the basis of the actual situation as it develops. It is true that even then it may not be possible for the Commission to indicate precise magnitudes of assistance to various States for the period of two (or three) years which would be the duration of its award. In that case, the Commission may lay down the proportions in which assistance is to be given to the various States. These proportions may be related to the current revenues of the Central Government in such a way that the total of the estimated allocations broadly corresponds to the current account surpluses of the Central Government (excluding the allocations themselves).

15.8 We are of the view that a Commission charged with these functions should be headed by a person of eminence and with a judicial background. Since the services of such a person, e.g. a Judge of the Supreme Court, are not likely to be available for more than a short period he may be invited to serve for six months or so and preside over the Commission during its award-giving phase. The other members (excluding the Vice-Chairman) could also be appointed for this particular period only i.e. the award-giving phase of the Commission. For the rest of the time, however, the reorganised Finance Commission may continue as a permanent body with a small permanent secretariat under a Vice-Chairman.

This body will undertake various studies regarding tax potential and expenditure trends of the States and, in particular, will be charged with the task of evaluating or co-ordinating the execution of plan programmes both in the States and the Centre. The reorganised Finance Commission will work in close collaboration with the Planning Commission. In order to provide a nexus with the Planning Commission, we suggest that one of the members of the latter should be appointed Vice-Chairman of the reorganised Finance Commission, and in that capacity, virtually be in charge of this permanent body during the non-award phase.



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CHAPTER XVI

Schemes of Basic National Importance

16.1 We have urged in the previous Chapter that the area of untied allocations should be enlarged and that of discretionary grants-in-aid reduced in bringing about a modified relationship between the Centre and the States. We consider that the latter category, i.e. 'tied' assistance, should be confined to a very few schemes of basic national importance. It is essential that they should not be too many, as in our view are today's "Centrally sponsored schemes" (a designation which, incidentally, we would avoid using for the schemes we have in contemplation). It is also necessary that, starting with very few, they should not then proliferate into very many. For that might amount to re-introducing by the back door the whole system of discretionary grants.

16.2 The idea of certain schemes being drawn up by the Central Ministries and sponsored for acceptance by the States originated during the Second Plan period. In order to facilitate acceptance, more liberal assistance was offered along with the schemes. Consequently, although the States had the option to accept or reject, few showed any reluctance to accepting these Centrally sponsored Schemes. Their number, however, was reduced during the Third Plan in the light of certain criteria which were laid down for such schemes:-

- (i) they should relate to demonstrations, pilot projects, survey and research;
- (ii) they should have a regional or inter-State character;
- (iii) they should require lump sum provision to be made until they can be broken down territorially; and
- (iv) they should have an overall significance from the all-India angle.

The future of these schemes has been examined recently by the Planning Commission in consultation with the Central Ministries and the State Governments. The subject was also discussed by the National Development Council. Thereafter, the Planning Commission have reduced the number of such schemes by transferring some of them - 36 in all - to the State Plans. The total outlay on the schemes so transferred will now form part of the Fourth Five Year Plan outlay of the States, the Centre's share of the Plan outlay on these schemes being available as Central assistance over and above the amount already agreed to for the States' Fourth Plan. We understand that the remaining schemes (about 90 in number) will, according to present thinking, continue to be Centrally sponsored. The Centre's share of the outlay on these individual schemes will be provided in the respective Plans of the Central Ministries; the States' share of the outlay will form part of the Plan outlays of the State Government; and assistance in the form

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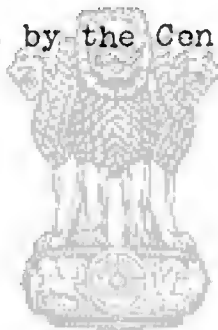
of loans and grants will continue to be given to the States in accordance with the existing pattern.

16.3 We consider the number too large in spite of the reduction. It is true that the listing of schemes as Centrally sponsored provides a convenient mechanism by which the identity and character of the individual schemes can be preserved. This is sometimes a significant advantage and is in contrast to the State Plan schemes whose distinct identity is lost by the merger of the schemes in the totality of the schemes under a Head of Development. At the same time, Centrally sponsored schemes have a number of other implications of their own. The States tend to accept such schemes without proper scrutiny from the point of view of either suitability or economy and sometimes even without being really interested, merely because their cost is met by the Central Government. Moreover, the acceptance of such schemes tends to have repercussions on the policies of the States in matters which are primarily under their jurisdiction. For these reasons, the point of view has been urged before us that the Centrally sponsored schemes should be abolished altogether. We feel there is much validity in this contention. But while we think this name should go, we consider it equally important to recognise that there is a minimal number of basically important schemes which, within constitutional limits and with, of course, the full cooperation of the States, the Centre must try its utmost to promote. We have in

mind, for example; (i) family planning and (ii) programmes of agricultural production based on high-yielding varieties of seeds. We feel that in such cases there should be tied assistance and the supervision that should go with "tied" assistance. This does not, however, mean that there should be a set pattern evolved at the Centre and obligatory on the States for every such schemes. On the contrary, once the objective in physical or other terms is agreed upon, considerable latitude should be left to each State to evolve patterns most suited to that State. The objective and over-all target would be all-India, while the pattern would be adapted to the conditions of the State concerned in consultation with the Centre. The identity of the schemes could be retained, even though they form a part of the State plans. Their number, as we have emphasised, should be kept as small as possible.

16.4 We do not envisage that the list of schemes of basic national importance, would at any given time be something immutable or permanent. The national priorities may undergo transformation by the change of circumstances; new items of higher priority may arise while items enjoying high priority at present may not retain their importance, having fulfilled their purpose. The position will have to be reviewed from time to time though not at too frequent intervals. The list itself will, no doubt, be drawn up in consultation with the National Development Council.

16.5 Central assistance in the form of 'grants' and 'loans' is also given to States for non-plan purposes. Instance of such assistance are grants for the Border Security Force, Employment Exchanges, Relief and Rehabilitation of displaced persons and loans for Police Housing Schemes and the construction of certain capitals. Both loans and grants have been given to States in connection with natural calamities. All these are outside the plan and the assistance has been mostly on a 'tied basis'. Such instances may continue to be regarded as a separate category and assistance provided as at present by the Central Ministries.



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CHAPTER XVII
THE NATIONAL DEVELOPMENT BANK -
ITS NATURE, SCOPE AND FUNCTIONS

17.1 It is in regard to the third category of assistance, viz., Central loans to States for financing identifiable projects in fields like power, transport, irrigation and manufacture that we suggest a somewhat radical departure from the existing practice. The proposal made here is that, in a phased manner and over the next few years, there should be built up a new institution, to be known as the National Development Bank, for the purpose of channelling long-term finance to such projects. The attempt, it will be noticed is -

- (i) to demarcate certain types of projects into a separate category, and
- (ii) in respect of that category, to replace existing arrangements by non-political, business-like and institutional procedures for the provision, from time to time, of investment and other long-term capital.

We may add that the contemplated arrangements would apply to both Central and State projects as long as these fall in the defined category.

17.2 From one important point of view, the justification for the proposal may be stated as follows:-

In the modified Centre-State financial set-up which we envisage, one aspect to which we have drawn attention is the cutting down of conditional or discretionary assistance to the minimum. At present the large bulk of assistance is discretionary, and there are literally hundreds of schemes for which the funds provided are conditional grants. Yet, there is not, and cannot be, adequate supervision on the part of the Centre in regard to the fulfilment of the conditions. More often than not, the conditions remain on paper, and what is promoted is irritation rather than implementation. Apart from other considerations, it is realistic to remove conditions which it is not practicable to supervise and which, on the whole, it may not be very important to enforce. But in this routine process, schemes of national importance as also schemes in which specific investment of a developmental type has taken place get treated like hundreds of other schemes, and there is no real machinery for ensuring that the grants or loan-funds are being properly utilised and the conditions, from time to time, properly fulfilled. Our concern, therefore, is to ensure appropriate supervisory arrangements - in conjunction with the financial arrangements - in those cases where it is really necessary, while doing away with conditions to the utmost in all other cases. There are obvious reasons why such arrangements, in the case of projects involving investment, should be non-political and institutional.

17.3 Moreover, the institution devised, besides being

development-oriented, has to be professional and business-minded. The projects in question have to yield a return. This may be relatively high in some cases or small in other instances. But it is important to ensure in every case that the return assumed when the project was sanctioned does in fact materialise. If this pre-condition is ignored, capital, already scarce, would tend to be used wastefully. The existing arrangements for disbursement of loans to such projects have been extremely unsatisfactory from the point of view of return on capital.

17.4 The proposed National Development Bank is designed to surmount, as far as may be, the difficulties mentioned above. Being a bank, it would, while granting financial assistance, initiate steps for effective supervision of the projects. Business principles would be observed to the maximum extent appropriate in sanctioning instalments of loans from time to time. This should also have the effect of making the project authorities more conscious of their responsibilities in respect of cost and return.

17.5 Three considerations have to be kept in view as regards the functioning of this Bank. First, this Bank should deal with loans and not also grants. Second, the assistance which might be purveyed by the Bank to the State Governments should be governed by the condition that the States should meet a specified part of the outlay. This is necessary in order to induce the States

to put in greater effort to raise resources for the projects undertaken within their jurisdiction. Third, there might be need to introduce softer types of loans on the analogy of the International Development Association - an affiliate of the World Bank. Such loans would mainly be for infrastructural projects like irrigation, transport, etc. where the social rate of return is higher than private return. The softness of loans would be in the form of liberal conditions governing the repayment schedule or the rate of interest to be charged on loans or both.

17.6 The broad sectoral as well as regional pattern of assistance would be determined by the Planning Commission. However, the assistance for individual projects - whether State or Central - would be left to the discretion of the Bank and would depend on the rational appraisal of the planned projects and their actual implementation.

17.7 Such a Development Bank would improve implementation in several ways:

- 1) The selection of projects would be done, as far as possible, on the basis of rational criteria evolved on the basis of Plan objectives;

- 2) It will ensure that the scrutiny of the techno-feasibility reports and the appraisal of the performance of the projects would be done with the critical eye of a banker and on considerations of merit and economic viability, financial returns, sound

businesslike management, etc.

3) The Bank would be able to identify the causes of delays and waste in the implementation of projects and render useful technical assistance to remove the deficiencies in the process.

4) In view of delays in implementation of some projects, the Bank would be in a position to switch over resources from such projects to other worthwhile projects and thus ensure optimum and effective utilisation of its resources.

5) The Bank would induce the public sector enterprises to formulate and implement projects in a businesslike way. By placing the responsibility squarely on the project authorities for servicing the loans and for amortising them, it will infuse a performance and cost consciousness in them and they will be obliged to run their projects on businesslike and commercial lines in order to secure the surpluses not only for paying interest charges etc. but also for paying dividend to the Central or State Governments as the case may be.

6) Scarce technical and managerial talents would be used with the maximum effectiveness.

7) Foreign governments and international agencies are likely to be more willing to extend assistance through a Bank run on business principles than through the normal administrative channels.

17.8 By centralising these functions, it would be possible to evolve a sound investment programme and ensure an optimum use of resources. As a result, the administrative and political organs of the Government would be able to concentrate more on their other functions and there would be a considerable gain in efficiency.

17.9 We have already stressed that the activities of the Bank should be enlarged in stages, for it would obviously not be able to deal with an outlay of a few thousand crores without adequate preparation initially and adequate planning thereafter. A good starting point may be the financing of expansion of the existing projects. Perhaps, also such projects as involve familiar techniques of production may be taken up as they will not make heavy demands on the technical personnel. After gaining some experience, the area may be extended to projects whose gestation does not take too long and where the return is relatively large. From among projects such as manufacturing concerns, hydro-electric schemes, irrigation schemes and so on, those which are of a manufacturing type may be taken up in the beginning. Once the expertise is built up and the size of operation expands, the National Development Bank can extend its functions to projects with more complicated techniques of production. Such projects as would not qualify for being financed by the Bank would continue as before to be financed by the Governments concerned, Central and State.

17.10 Since the National Development Bank would not only be a financing agency but also an institution which would

mobilise savings, it will have to address itself to ways and means to raise, on its own, the resources from the market. However, in the beginning, it may not be possible for the Bank to undertake a borrowing programme on any large scale either internally or abroad. Therefore, the resources of the proposed institution would have to be provided for in the Central Budget. As time goes on, and the area of its operations is further enlarged, the Bank can raise loans in the domestic market as well as abroad.

17.11 We may now refer in general terms to some of the organisational aspects of the National Development Bank. The equity capital should be wholly subscribed to by the Government of India. The general superintendence and direction of the affairs and business of the Bank should vest in a Board of Directors which, with the assistance of an executive committee, may exercise all the powers of the Bank. In discharging its functions the Board should act on business principles with due regard to the interests of national development. On questions of broad policy, it should be guided by such directives as may from time to time be given to it by the Government of India. The Bank may appoint one or more Advisory Committees for the purpose of assisting it in the discharge of one or more of its functions and in particular for the purpose of ensuring that due regard is paid to the requirements of particular areas.

17.12 The Bank may have either a part-time or a whole-time Chairman. He should be a person pre-eminent in industry, commerce, finance or banking and unconnected with Government. It should also have a Vice-Chairman, who should be part-time if the Chairman is whole-time, and whole-time if the Chairman is part-time. In addition, there should be a Managing Director with appropriate financial and banking experience. The Board of Directors should consist, in addition to the Chairman, Vice-Chairman and Managing Director, of one Member of the Planning Commission, one Deputy Governor of the Reserve Bank of India, a Finance Secretary of the Government of India and three other Directors. Where the Vice-Chairmanship is part-time, the Member of the Planning Commission who is on the Board might appropriately be given this assignment thus ensuring better co-ordination with the Commission.

17.13 The bonds of the Bank would be fully guaranteed as regards the payment of principal and interest by the Government of India. The Bank should be prohibited from acceptance of deposits from the public on demand or on the expiry of fixed periods.

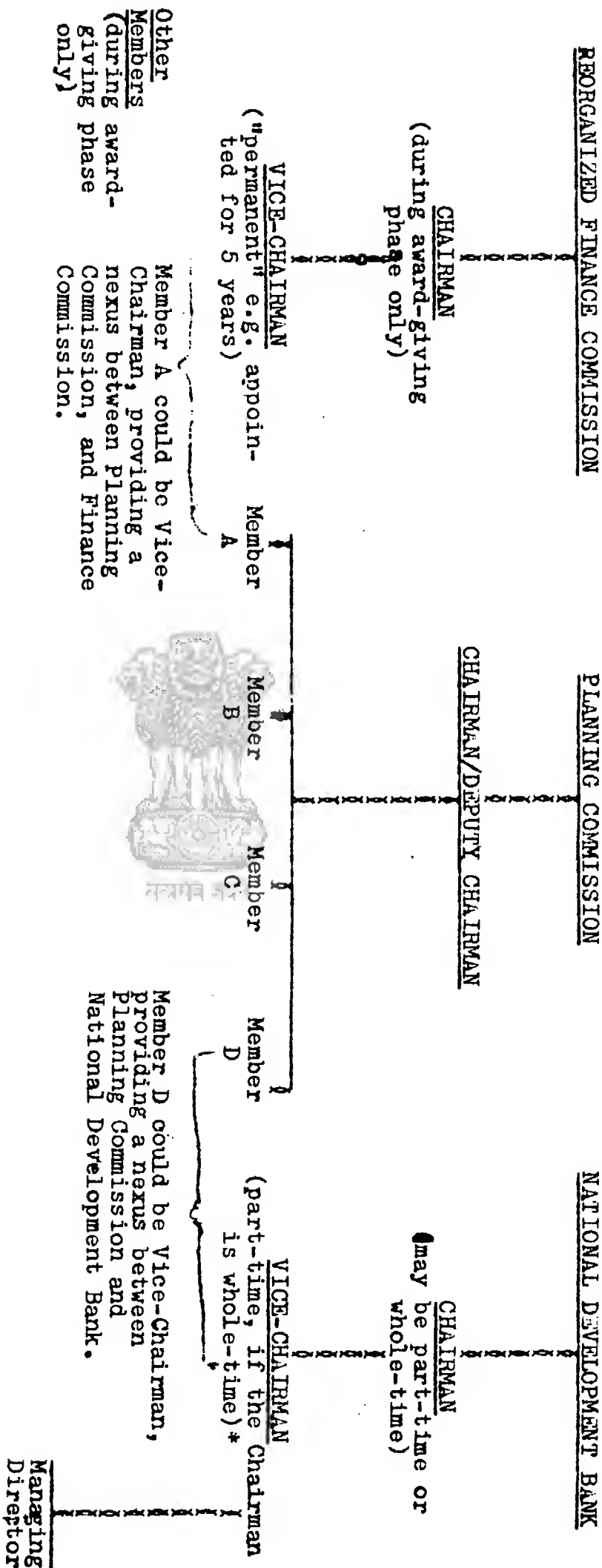
17.14 The National Development Bank should have adequate trained staff to appraise projects as well as supervise and watch the performance of selected projects. The utmost care should, however, be taken to avoid duplication of staff and of work. At present, there is a large body of trained personnel with the necessary expertise which is suitable for this purpose but which is dispersed over the various

Central Ministries and the State Governments. Some of them can be redeployed in the new organisation; others can be made use of where they are. Further the Bank should utilise specialised consultancy and other services to the maximum extent possible on the analogy of the Industrial Development Bank of India, the Industrial Credit and Investment Corporation of India and ^{other} similar financial institutions. This would help it to economise on overheads.

17.15 We have indicated the interlinking which, at the organisational level, would exist between the National Development Bank and the Planning Commission on the one hand, and the Planning Commission and the reorganised Finance Commission on the other. The co-ordination between these three bodies should result both in more realistic planning and more effective implementation. The accompanying diagram (annexed to this Chapter) illustrates the main features of the schemes of coordination which we have in mind.

ANNEXURE

Diagrammatic explanation of some of the proposals in Chapters XVI and XVII



*If the Chairman is part-time and the Vice-Chairman has therefore to be whole-time, Member D of the Planning Commission would be merely a member of the Board of the National Development Bank. There would still be a nexus between the two bodies.

CHAPTER XVIII
THE BORROWINGS OF THE STATES

18.1 One matter of importance that remains to be dealt with as having a general bearing on Centre-State financial relations is the borrowings of State Governments from (a) the Reserve Bank of India and (b) the public. Apart from its relevance, any substantial borrowing by the States from the Central bank of the country has monetary and economic implications which must be of as much concern to the States as to the Central Government and the Reserve Bank. The same is also, of course, true of certain types of borrowings from the Reserve Bank by the Central Government. A different set of considerations arises in respect of borrowing - either by the States or by the Centre - from the investing public in terms of Government securities. We propose in this chapter to deal with certain aspects of both these types of borrowings.

18.2 Under the existing constitutional provisions, viz., Article 293(3) and (4), the consent of the Central Government is required to all borrowings by a State Government if the State has loans outstanding for repayment to the Centre. This consent may be given subject to such conditions as the Government of India may consider it appropriate to impose. Since, generally speaking, all States are indebted to the Centre, the borrowing programmes of State Governments are in

effect subject to the approval of the Central Government. It would be useful here to outline briefly the procedures governing the borrowing transactions between the State Government and the Reserve Bank.

18.3 First there are the normal ways and means advances. These are almost automatic. They are made to the States at their request and are subject to certain limits which are related to the minimum balances that each State is required to keep with the Reserve Bank. Under the arrangement now in force, the States can borrow from the Reserve Bank upto twice the amount of the minimum balances.

18.4 Secondly, there is special ways and means accommodation. This is granted against the hypothecation of the Central Government securities, subject, in theory, to a limit of Rs. 2 crores. In practice, the limit is not adhered to and the States can borrow a larger amount provided they can pledge Government securities of the requisite value with the Reserve Bank. Loans of this kind, though normally repayable within three months, are renewable after the expiry of the period. The debtor Governments clear the amounts borrowed either by the sale of the securities pledged or by making good the amount out of their budgetary receipts.

18.5 Thirdly, there is the form of irregular borrowing which has come to be known by the general term, 'Overdrafts'. The overdrafts are unauthorised in the sense that no prior arrangements in respect of them are entered into between

the borrowing Government and the Reserve Bank. They result when the State Governments draw cheques on the Reserve Bank in excess of what they are authorised to borrow at the particular time. In view of the special, and in some ways delicate, relationship between the Reserve Bank and the State Governments, the former is understandably reluctant to dishonour their cheques. Its usual practice in these circumstances has been to draw the attention of the State Governments to the debit balances and to request them to clear them as quickly as possible. This is sometimes followed by discussions with the States. The Central Government is also kept informed of the position. Sometimes the overdrafts are cleared through adjustment against Central assistance to the concerned State in relation to Plan schemes sanctioned by the Government of India. For obvious reasons, the auditors insist on the unauthorised overdrafts being cleared by the end of the accounting year of the Reserve Bank. Where the defaulting State Government is not in a position to do so, the Central Government takes over the debit balance. Thus the State Government's debit is ultimately transformed into a liability of the Centre, which has perforce to treat it as a special loan to the concerned State. Most of the overdrafts, especially those of long duration, not only contravene the provisions of the Reserve Bank of India Act, but are also not in conformity with the agreement entered into

between the State Governments and the Reserve Bank of India. While overdrafts for short periods may be due to a temporary lag in the inflow of receipts, those continuing over a long period must be attributed to the persistent imbalance between resources and outlays. It is clear that, for more reasons than one, they present a serious problem.

18.6 The following appear to be some of the principal causes of the State Government's overdrafts:

(i) The disbursing offices of the State Government - consisting of treasuries and sub-treasuries, both banking and non-banking - are widely spread over the length and breadth of the State. In the absence of proper coordination and control, they may draw amounts from the Reserve Bank which in the aggregate are, at a given point of time, in excess of the balances to their credit.

(ii) Temporary shortfalls in the State's resources on account of payments made to other State Governments or the Central Government.

(iii) Delays in the receipt of Central assistance.

(iv) Large and unexpected expenditure - e.g. on account of floods - which has not been provided for.

18.7 It is clear that the last three causes do not present any very serious problem. They are ad hoc and the ensuing dislocation can be removed either immediately or over a relatively short period. It is the first of the different factors listed above - the one relating to disbursement through a wide-spread net work of banking

and non-banking treasuries-that is relatable to a more chronic situation and needs more elaborate remedies. An arrangement that might perhaps be considered in this connection is that the various disbursing officers should be given limits of the grants which they can spend, as soon as the voting for grants is completed. In order to leave some leeway, the Finance Department could stipulate limits lower than the amounts voted for. At the end of each month the disbursing officer should reconcile the figures of expenditure in consultation with the concerned Accountant General and report them to the controlling officers in the Finance Department. An abstract of expenses by major heads could also be obtained by the controlling officer from the Accountant General concerned for checking the pattern and magnitude of expenditure with the grants voted. In this manner some control over the disbursements could be exercised. We understand that such an arrangement is operating in one State. Its efficacy could be examined along with the feasibility of extending it to other States.

18.8 Another remedy may be to put **statutory** limits on the States' borrowing from the Reserve Bank. If, for instance, it is provided by a suitable provision in the Reserve Bank of India Act that the State Governments' borrowing from the Reserve Bank should not go beyond a certain proportion of their current revenue resources at any point of time, it would be an important legal

safeguard against the overdrafts of the State Government. Such an arrangement would also have the advantage of a certain degree of flexibility. As the resources of the Government increase the absolute level of permitted borrowing would go up automatically. This practice is prevalent in many countries such as Malayasia, the Philippines, Canada, and West Germany.

18.9 We would at the same time stress that such a restriction should also apply, mutatis mutandis, to the Central Government in respect of its borrowings from the Reserve Bank. Under the existing system, the Central Government is free to borrow from the Reserve Bank to any extent on the basis of 'ad hocs' or by the issue of dated securities. Though such a practice is intended to help the Centre in tiding over their temporary ways and means difficulties, it tends to persist and is thus an even more significant way of deficit financing than the States' overdrafts.

18.10 Another alternative might be for the State Governments to have for their banker, not the Reserve Bank, but the State Bank and its subsidiaries. The corollary of this would be to transfer the balances of the State Governments to these banks. By so doing, the credit transactions of States would become subject to the rules and regulations and business discipline that goes with commercial banking. The State Bank, for its part, is bound to insist on adherence to limits since, unlike the

Reserve Bank, it is in no position to extend virtually unlimited credit. There is nothing unusual in this procedure. In the U.S. for instance, the States keep their balances with the commercial banks and draw from them at need.

18.11 We may now discuss certain issues connected with the State Governments' borrowing from the public. At present, the States go individually to the market, but there is a certain amount of co-ordination in that the Reserve Bank's clearance has to be sought as to the size and terms of the proposed loans.

18.12 However, the fact remains that State loans have not been conspicuously successful. We would here draw attention to three important features. First, the securities of certain States are quoted at heavy discount. It should be realised that the presumption that all Government loans should have the same degree of appeal to the investing public is not true in practice. The market for the State Government loans is not one entity. For one reason or another, the public have come to place the credit-worthiness of certain States higher than that of the others. Furthermore, some of the State Governments are known to exert pressure to get their loans subscribed to within the stipulated period of flotation. A frequent result is that such loans are heavily discounted immediately after flotation.

Second, the Central Government loans

command a higher market value than the State Government loans.

Third, the main purchaser of the State Governments loans are the State Governments themselves. The proportion of the subscription to these loans, either on a reciprocal basis or by the borrowing States themselves out of their own funds, has gone up substantially and is now around 28 per cent. This implies that, if brokerage etc. are taken into account, one centralised loan programme would be cheaper than the flotation of a number of State loans.

18.13 In view of this, we feel that it would be a good idea if the borrowing of all the State Governments was centralised. It is true that such an experiment was tried on two occasions - in 1954-55 and 1963-64- without much success. Yet we feel that it should be given a further and more systematic trial. Alternatively, it is necessary to ensure greater preliminary care on the part of the Central Government and the Reserve Bank in the matter of fixing the quantum of each State loan. Past experience indicates that some of the State Governments, after having been advised by the Reserve Bank, canvass for a higher figure with the Central Government; and instances are not wanting of the Central Bank having been subsequently persuaded to accept higher figures in some cases. There is a need for more effective co-ordination in this matter between the Reserve Bank and the Government of India.

18.14 So far we have confined ourselves to market loans

Another category of 'borrowings' is represented by small savings. Though this programme is organised by the Central Government, the States have a stake in it, insofar as they are given $66\frac{2}{3}$ per cent. of the funds raised by them in the form of saving certificates within their jurisdiction. We are of the view that the Small Savings Scheme has not succeeded in its principal aim of fostering new savings. Most of the savings come from the higher income groups or from Provident Funds, etc. In such cases the Small Savings Scheme is merely a convenient alternative outlet for investment which would have been made in any case. As far as genuine small savings are concerned, it is observed that the cost of sale of certificates to the low-income groups is even higher than the net proceeds from the sale of certificates to them. The organisation of small saving instruments for this purpose is thus a somewhat costly operation. Such success as has been achieved by small savings has been through the scheme of post office savings deposits. It will be desirable to encourage this particular scheme through suitable measures.

C O N C L U D I N G
S E C T I O N



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CHAPTER XIX

A C K N O W L E D G E M E N T S

19.1 It remains for us to make grateful acknowledgement of the assistance we have received from a large number of individuals and institutions. The Working Groups - on Performance Budgeting and Centre-State Financial Relations- have laid us under obligation by the thoroughness with which they have discharged the tasks entrusted to them. We are thankful to them and to each member, individually, of the two Groups as well as of the research team of the Indian Institute of Management, Ahmedabad.

19.2 Further, our thanks are due to the Planning Commission for permitting Sarvashri E.R.K. Menon, S.S. Viswanathan, and A. Premchand, to the Ministry of Finance for permitting Shri A.G. Krishnan, and to the Indian Institute of Public Administration for permitting Dr. M.J.K. Thavaraj, to serve on the Working Group on Performance Budgeting. We would thank the same Institute for having spared Shri K.L. Handa for conducting certain case studies. We are grateful to the University of Bombay for having permitted Dr. D.T. Lakdawala to head our Working Group on Centre-State Financial Relations. We are also grateful to the Reserve Bank of India for having agreed to nominate Shri S.D. Deshmukh, Dr. V.V. Bhatt and Dr. D.R. Khatkhate, and to the Government of Maharashtra for allowing Shri D.G. Tungare and

Shri K. Ramakrishna Iyer, to serve as members of the same Working Group. We are thankful to the Indian Institute of Management, Ahmedabad, for the readiness with which they organised the research study on performance budgeting.

19.3 We would thank the Central Government, State Governments, Public Sector Undertakings, Chambers of Commerce and other institutions and individuals who have sent replies to our questionnaire and otherwise assisted us in our enquiry. Our special thanks are due to the many officers, Central and State, who have participated in the several discussions we have held at Delhi and elsewhere.

19.4 We record our appreciation of the assistance we have received from Shri J.C. Luther, the Secretary of the Study Team. From our colleague, Shri N.S. Pandey, we have not only received considerable assistance but have derived advantage from his long association with financial administration. To him and to the staff working under him, including Sarvashri B.L. Gaur, N.K. Andley and S.D. Batra, we would express our thanks as also our warm appreciation of the able and conscientious work which has gone into the preparation of the material placed before us.

CHAPTER XX

SUMMARY OF OBSERVATIONS AND RECOMMENDATIONS.

Introduction:

1. Two of the basic requirements of administration, of which financial administration is only a part, continue to be efficiency and economy within the framework of planned development, parliamentary control and federal inter-relationship. But efficiency and economy are themselves aspects of action or performance; and if there is one requirement today which is more important than any other, it is that policies, programmes, and administration should all be oriented to performance. (Para 1.5)

2. Since that economy is costly which consists in doing nothing, our suggestions concerning control - whether by Parliament or by the Finance Ministry - aim at preserving initiative and delegating real authority. (Para 1.7)

3. In the context of the changing requirements of the Centre-State relationship, somewhat radical modification is needed in the Centre-State financial procedures, institutions and concepts. (Para 1.8)

4. Not only are economy and efficiency all the more necessary in the context of planned development; together, these two factors make it essential that projects which involve large developmental investment

should be completed without undue delay and extravagance and, above all, in practice yield the financial return on the expectation of which they have been formulated and sanctioned. If institutional measures are necessary for this purpose, they should be devised and adopted. (Para 1.9)

Objectives of a Budget:

5. Besides being the most important annual item on the agenda of Parliament, the budget serves a number of purposes, fiscal, financial and economic, administrative, managerial and developmental, in terms of each State or of the country as a whole. It is a document for parliamentary action and an instrument of parliamentary control. It is a management tool and a basis for administrative delegation. It sets out a programme of development and enables the adjudgement of performance. These objectives are not mutually exclusive. But, if there is one over-riding need today it is that all governmental processes - including the budgetary process - should be oriented to action and performance; action that achieves optimum results, and performance that involves not more than reasonable cost, effort and time. (Para 2.4)

Performance Budgeting:

6. We recommend that necessary steps for the introduction, in a phased manner, of performance budgeting

should be initiated at an early date..... It is of course, necessary that adequate preparatory steps should be taken for the introduction of the system. The following steps are recommended:-

(i) The Finance Ministry should assume responsibility for introducing the system and coordinating the various stages;

(ii) In the phased application of this system both at the Centre and in the States, priority may be given to departments and organisations which are in direct charge of programmes or activities (developmental or other) involving large expenditures.

(iii) The analysis of the functions and programmes of the departments selected may, as suggested by the Working Group, be entrusted to a team of officers.

(iv) A suitable training scheme may be devised for those who, at different levels will be concerned with the introduction of the scheme; and a manual of instructions on the subject might be prepared as soon as practicable.

(v) Appropriate changes in the accounting system would be needed in this connection. (Para 3.6)

Financial Year:

7. We have thought it desirable to analyse at some length the practical implications of the various criteria to be applied for judging the suitability or otherwise of a financial year commencing on (i) 1st April as at present, or (ii) 1st July, or (iii) 1st October, or (iv) 1st January. These criteria are

(i) accuracy of revenue estimates in the budget; (ii) accuracy of expenditure estimates; (iii) efficacy of performance; and (iv) convenience of legislators and administrators.

Our conclusion is that, if the status quo is to be changed, the balance of advantage would lie in favour of 1st October, more especially from the point of view of performance on which we have laid emphasis throughout the report.

Budget Estimates:

8. Various methods, not mutually exclusive, are employed in the scientific forecasting of revenue. The "Direct Valuation" method is the most comprehensive one, but depends for its success on the coverage and accuracy of the statistics available. The two Boards should review, from this angle, the adequacy of the statistical data now available to them and take measures to supplement them where necessary.

(Para 5.4)

9. Some of the causes of overestimation of expenditure or of underspending are psychological. These are explained. Other factors underlying delayed performance pertain to departmental, including financial, procedures; the need to get clearance from a multiplicity of agencies; defaults on the part of contractors, delays in receipt of supplies of materials, and procedures regarding the release of foreign exchange.

(Para 5.5)

10. We consider that managerial techniques such as PERT (Programme Evaluation and Review Techniques) and

C.P.M. (Critical Path Method) should be introduced as early as possible in Government projects and Government Departments, especially those concerned with the execution of relatively big schemes. Among other things, the adoption of these methods should lead to a much larger measure than at present of calculated control over points of crucial delay and in the same process to a much more reliable estimate than now obtains of the twin factors of time and expenditure. (Para 5.6)

11. The Ministries, Departments or Offices should have well-equipped Budget Cells. This would eliminate inaccurate estimation due to out of date data, imperfect techniques and, lastly, inadequate familiarity with the practical aspects and vicissitudes of the schemes and projects for which the estimates are framed. (Para 5.6)

Budget in Parliament:

12. In the altered circumstances, the question of reviving the Standing Finance Committee to examine items for inclusion in the budget estimates need not be pursued. (Para 6.2)

13. The device of a Committee of the Whole House to discuss the budget would be an unnecessary refinement. (Para 6.3)

14. The allotment of more time for discussions on the budget, if thought necessary, could be provided by

Parliament by suitable regulation of its internal business. (Para 6.4)

15. We recommend that, as a rule, the Minister in charge should open discussion on the budget estimates of his Ministry and explain the policies underlying the estimates, the physical programmes planned, and the performance in the preceding year. (Para 6.5)

16. It is desirable that specific dates should be fixed by which the Appropriation Accounts and Audit Reports thereon should be submitted - (a) by the Comptroller and Auditor-General to the Finance Ministry; and (b) by the Finance Ministry to the Parliament. We recommend that a provision to this end should find a place in the proposed Bill governing the functions and duties of the Comptroller and Auditor-General; the Comptroller and Auditor-General should be required to forward his report to the Finance Ministry by a definite date say, 15th January and the latter to submit it to Parliament by 31st January. These suggestions would apply mutatis mutandis to the State Governments also. (Para 6.7)

Budget, Plan and Economic Analysis:

17. The lack of direct correlation between the Plan and Budget heads not only renders it difficult and cumbersome to follow with real understanding the financial provisions made in the budget for plan schemes but in relation to the schemes in State Plans gives rise

to special problems in the matter of regulating Central assistance. It is, therefore, necessary that a proper link should be established between the budget heads of account and the heads of development. (Paras 7.1 & 7.2)

18. A greater measure of uniformity in classification should be attempted to achieve better correlation and necessary modifications made in the heads and Sub-heads, etc. of accounts. We suggest that the position be reviewed in consultation with the Comptroller and Auditor-General and such changes introduced as are appropriate from this point of view. (Para 7.3)

19. The link between the Plan schemes and the budget heads could be provided, for instance, by means of code numbers to be assigned to each scheme on the pattern of what is being done by U.P. Government. This could be brought out in a separate document as a supplement to the budget literature. (Para 7.4)

20. In view of our recommendation regarding Performance Budgeting in Chapter III, both the heads of development and the major and minor heads would need to be recast to bring about a better correlation between the Plan and the Budget documents. (Para 7.5)

21. The main utility of the economic classification of ^{the} Central Government Budget is that ^{it} promotes a better understanding of the economic impact of Government's

operations. To be really useful, the scope of this exercise should^{be} extended to the budgets of the State Governments as also to non-departmental enterprises of both the Central Government and State Governments. (Para 7.8)

22. As in other advanced countries, economic classification should be integrated with the budgetary process itself. We, therefore, suggest that an economic analysis be presented of the budget estimates of each department. (Para 7.9)

23. The efforts that are being made by the Central Statistical Organisation for compiling official series of savings and investment together with the recommended enlargement of the scope of economic classification would fulfil much more adequately than at present the needs of economic analysis and policy formulation. (Para 7.10)

Lapse of grants:

24. If the Ministries or Project authorities could be given some assurance, albeit informal, by the Finance Ministry/department that underspending in one year would not prejudice the budget estimates for the next year, the Department's reluctance to surrender funds in time would tend to diminish. (Para 8.7)

25. Better phasing and programming of expenditure on a project, and the introduction of performance budgeting which would relate financial outlays to physical achievement,

would also tend to reduce the incidence of the lapse of funds. (Para 8.8)

26. A prompt system of communication of the new budget grants is necessary in all cases. Besides this a part of the difficulty could be met by a more liberal recourse to the system of Vote on Account. (Para 8.9)

Lump Sum and Token Grants:

27. The real meaning of "token Grant" should be kept in mind and a token grant asked for only when funds required for new schemes can be found by reappropriation, but the approval of Parliament has to be obtained since it constitutes a new service. (Paras 9.2 & 9.3)

28. There should be a total ban on the inclusion of lump sum provisions in the budget. Important schemes which are not yet ready in detail for execution could be brought up in supplementary Demands and less important ones could be left over for the next regular budget. (Para 9.4)

29. The administrative Ministries can and should take steps to obtain the clearance of their budget proposals from the Finance Ministry well before the final date stipulated in the budget calendar. Such proposals should be staggered over a longer period and should not clutter the Finance Ministry towards the end. (Para 9.4)

30. Lump sum provisions should be regarded as permissible only in the most exceptional circumstances, e.g., where urgent measures have to be improvised for meeting an emergency. These could also be justified for meeting preliminary expenses on a project scheme where item-wise estimates could not be worked out. For such purposes the amount of contingency funds might be increased both at the Centre and the States. (Para 9.5)

31. Provisions are in most cases not thought of in terms of programmes, or expenditure in terms of activities. On the introduction of performance budgeting there is expected to be some change in this general attitude. A Department which thinks in terms of performance budgeting is unlikely to ignore the action content of scheme for which a large overall provision is asked for. (Para 9.6)

Review of Expenditure:

32. It is necessary to take notice of the various inadequacies revealed in the present procedure of expenditure reporting. A good system of progress reporting should provide a basis for a comparison of the current progress against the past and the projected schedule of work. Specifically, the object of expenditure reporting should be as follows:-

- (1) accounting data should facilitate the formulation of a policy and also throw up material that will make possible the assessment of the working of the policy.

- (ii) it should also ~~render~~ the action of each agency accountable to the higher agency or to the Legislature and through it to the public in the ultimate analysis.

(Paras 10.2 & 10.3)

33. An important requirement of planned economic development is a system of data reporting that would establish a rapport between the financial and physical aspects. The reporting system should be increasingly oriented to meet the requirements of performance budgeting. In a matter like financial reporting, modern techniques should be adopted over as wide an area as possible. In the context of increased financial responsibility of the administrative Ministries and Departments, there would be greater need of adequate internal reports for the use of both the Department and the Finance Ministry.

(Para 10.4)

34. The Comptroller and Auditor General and the administrative Ministries should in consultation take steps to ensure that expenditure figures are submitted punctually at all levels of the organisation. (Para 10.5)

35. For post-budget review of expenditure by the Finance Ministry the form of expenditure statement should be amplified in several respects and these should be submitted more regularly.

(Paras 10.6 & 10.7)

36. Steps should be taken to remove the difficulties of administrative Ministries in the matter of watching the progress of expenditure. The real solution would lie in transferring the responsibility for maintenance of accounts to the executive agencies. The system of accounting has to be such that the Ministries and other administrative authorities below them, can discharge their respective responsibilities in as full, unhampered and effective a manner as possible. (Para 10.8)

Delegation of Financial Powers:

37. A scheme of delegation of financial powers which does not become operative until the last detail is approved by the Finance Ministry is unsatisfactory. Once the preliminary feasibility report has been prepared and accepted by Government the administrative Ministries should be permitted to sanction expenditure on essential preliminary items subject to certain limit,^a proportion or percentage of estimated cost. (Para 11.8)

38. Delay occurs in the process of scrutiny and examination by Finance. A time limit of, say, four to five months should be laid down within which the approval of the Finance Ministry to a project or a scheme should be accorded, failing which there should be provision for the matter being automatically brought for decision before a Committee presided over by the Cabinet Secretary. (Para 11.9)

39. The Ministry of Finance should play a more positive role in the matter of grouping of schemes and obtain for the purpose of approval the lists of related schemes (within which re-appropriation powers are vested in the administrative Ministry) at the time of formulation of the budget. (Para 11.10)

40. A review of the rules for the delegation of financial powers may be made with a view to vesting more powers in the administrative Ministries in the matter of negotiating contracts and placing orders for materials and supplies. (Para 11.11)

41. In the matter of creation of posts we recommend greater over-all control. Many of the Work Study Units, on whose advice posts can be created, have not built up the expertise required for their becoming effective advisers in this respect. We are of the view that this function should be entrusted to a well-trained staff inspection unit composed of officers with adequate training in methods of work study, work measurement, etc. The new unit should be located in the Ministry of Home Affairs or in the Cabinet Secretariat. (Paras 11.12 & 11.13)

42. In cases of emergency giving rise to sudden increase in work, the Ministries and heads of departments should have powers to create temporary posts for short periods not exceeding three months in all. (Para 11.14)

43. Except in the case of creation of temporary posts, in emergent circumstances, there should be no powers of re-appropriation which results in the enhancement of the provision for pay of officers, pay of establishment. (Para 11.15)

44. A provision made for a "Non-Plan" item and not utilised should be allowed to be re-appropriated for a plan scheme (under the delegated powers) obviating the necessity of making a reference to the Finance Ministry in such cases. (Para 11.16)

Role of Financial Adviser:

45. There is an overriding need for prompt decision and speedy implementation. From this point of view, it is of vital importance that the responsibility for the execution of the programmes and for delivering the goods should rest squarely on the Ministries and departments concerned. It is in the discharge of these responsibilities and as an integral part thereof that the need arises for internal financial advice. (Para 12.3)

46. The responsibility of the Secretary of the Ministry should remain unimpaired, and he should, therefore, have the power to overrule the Financial Adviser, where necessary. There will be no place for a Financial Adviser outside the Ministry in the arrangements we contemplate (Para 12.4)

47. There is a definite advantage in the Financial Adviser being appointed with the concurrence of the Finance Ministry. The annual assessment of his work should be made by the Secretary of the administrative Ministry and the report of the Secretary Expenditure should also be obtained. The Finance Ministry should have an overall and coordinating interest in the careers of Financial Advisers. (Para 12.4)

48. The Financial Adviser is expected to be a part of the top management team of a Ministry/Department. The Secretary will attach the highest importance and give the most careful consideration to the views expressed by the Financial Adviser. The relationship between them should be that of senior partners in a common enterprise. (Para 12.5)

49. There would be great advantage in providing for the formulation of a uniform set of rules for the guidance of administrative Ministries in the matter of financial consultation/procedures. (Para 12.6)

50. It should be obligatory on each administrative Ministry to have a Financial Adviser though on considerations of work load, etc., it should be open to Government to entrust to one official the work relating to more than one Ministry. (Para 12.6)

51. The Finance Branches of the administrative Ministries should be strengthened and staffed with trained and qualified personnel.

(Para 12.6)

52. The Finance Ministry should not normally entertain references falling within the delegated sphere of an administrative Ministry.

(Para 12.6)

53. The recommendations relating to appointment of Financial Advisers and strengthening of Finance and Budget Cells might involve some extra expenditure, but this would be well worth incurring and would be well repaid by the improvement and efficiency of financial management

(Para 12.7)

54. The Financial Adviser should come to their assignment with a background of administrative experience and at an appropriate stage should be given orientation in the functions and duties thereof.

(Para 12.8)

55. Periodic interchange between the financial wing and other wings of administration will not only enrich the experience of those who are thus interchanged but also, in the long run, make for sounder finance as well as sounder administration.

(Para 12.9)

Control by Parliament:

56. Parliament's time is valuable. In so far as Committees draw Parliament's attention to specific matters, these matters must be important enough to justify Parlia-

ment devoting time and attention to them. In the context of Parliamentary control the matters in question may be classified as (a) accounts - the proper spending of moneys sanctioned by Parliament; and (b) performance - the effective implementation of programmes approved by Parliament. Both in regard to proper spending (accounts) and effective implementation (performance), only the most important items should be brought to the notice of Parliament. (Para 13.10)

57. The Public Accounts Committee will, it is expected, confine its attention, and therefore, its comments, to items of outstanding importance. It will not deal with minor matters including relatively small irregularities in such a manner as to lay itself open to the criticism that it is helping to hinder initiative. It will, of course, continue to comment upon and draw pointed attention to instances of major irregularities. (Para 13.10)

58. Nothing is easier to inculcate than the habit of not taking decisions. And those hitherto accustomed to take decisions - and therefore risk - might hereafter desist from taking action if the only result, in the event of something going wrong, is adverse notice by the Public Accounts Committee and a blaze of undesirable publicity. (Para 13.10)

59. The Public Accounts Committee should. take over the expenditure side of the public undertakings. That leaves^{out} performance, viz., programmes, actions, and results, not only of Departments but also of public undertakings. This could well be dealt with by one Committee. (Para 13.10)

60. The Public Accounts Committee should, as has been the case in the past, refrain from taking cognisance of matters involving administrative decision or policy formulation unless these have been specifically reported to Parliament by the Comptroller and Auditor General in his audit report. (Para 13.11)

61. The review of performance in relation to budgeted programmes could best be done by a single Committee of Parliament, which may be called the Performance Committee. The Performance Committee could have two wings, one dealing with the performance of the Government Departments and Ministries and the other with the performance of public sector undertakings. It would be assisted by an organisation or group of experts in examination of the cost and efficiency aspects of the projects etc. (Para 13.12)

62. The area of operation of the Public Accounts Committee would be enlarged to include the appropriation accounts and audit report thereon relating to public sector undertakings also. (Para 13.13)

Changes in Perspective

63. The procedural aspects of Centre-State financial relations with which we are literally concerned cannot be considered in isolation from institutional aspects. In the context of the changes in substance of the Centre-State financial relations, it is necessary to evolve clearly defined objectives of Central assistance to States.

(Para 14.1 to 14.6)

64. If these objectives are to be fulfilled, it will be necessary to reduce considerably the proportion of the discretionary element in Central assistance; the unconditional or "untied" element of assistance would then increase. The States have to be told beforehand with reasonable certainty of the size of untied assistance over a period.

(Para 14.7)

65. Within the broader framework of major objectives and major strategy, the Plan has hereafter to possess two characteristics: (1) flexibility in terms of the States and (2) adaptability in terms of changing economic conditions. Consequently, it would be desirable to review the size of the untied assistance, not every five years, but at more frequent intervals, say, once in two or three years.

(Para 14.9)

Finance Commission

66. One body, and not two different ones should take a

view of both Plan and non-Plan expenditure and of all available resources in order to arrive at an appropriate pattern of allocation to States. (Para 15.3)

67. A reorganised Finance Commission should be entrusted with the total task of having a view of both Plan and non-Plan expenditure both Central and State and making the requisite allocation to the States. (Para 15.3)

68. The total Central assistance to States may be classified as follows into three categories:

- (i) Untied assistance covering the existing statutory grants and all assistance generally, with the exception of the two specified below,
- (ii) Assistance earmarked for a very small number of schemes of basic national importance, and
- (iii) Assistance for financing projects in certain major fields of development such as power, irrigation, transport and manufacture,

(Para 15.5)

69. Assistance for the first category should be untied and automatic.

The total quantum of assistance should be determined on the basis of the current account surpluses of the Central Government. It is necessary that appropriate criteria for allocating assistance of this type should be devised and this function should be vested in the reorganised Finance Commission which should be a permanent body. (Para 15.5)

70. In addition to its present functions relating to the devolution of taxes, the reorganised Finance Commission would devise criteria for allocating untied Plan assistance among the various States. A major portion of assistance may have to be given on criteria relatable to population, area and relative backwardness, and the remaining assistance on criteria relatable to the State's Plan and its performance. (Para 15.5)

71. The re-organised Finance Commission will have to review the achievements of each State, particularly in the agricultural and other specified spheres. It would be desirable that the awards of the Commission are given at intervals which are neither too long nor too short. Two successive awards, one for two years and the other for three years, together coinciding with a particular Plan period, might be suitable.

(Para 15.6)

72. The reorganised Finance Commission would take full account of (a) the Plan investments and estimates, (b) extent of the total resources available, and (c) the proportion which might be set aside for allocation to States.

(Para 15.7)

73. We are of the view that the reorganised Finance Commission should be headed by an eminent person with a judicial background, who may be invited to serve for six months or so and preside over the Commission during its award-giving phase. The other

members (excluding the Vice-Chairman) could also be appointed for the particular period only. For the rest of the time the reorganised Finance Commission may continue as a permanent body with a small permanent secretariat under a Vice-Chairman. To provide a nexus with the Planning Commission, we suggest that one of the members of the latter should be appointed the Vice-Chairman of reorganised Finance Commission. (Para 15.8)

Schemes of Basic National Importance

74. Tied assistance should be continued to a very few schemes of basic national importance. (Para 16.1)

75. There should be a minimal number of basically important schemes which the Centre must try its utmost to promote, for example, (i) family planning, and (ii) agricultural programmes in relation to high yielding seeds. The objective and overall target in respect of these schemes would be all-India but the pattern would be adapted to the conditions of the States concerned in consultation with the Centre. Their number should be kept as low as possible and their identity retained. (Para 16.3)

76. The list of such schemes of basic importance would be liable to review from time to time by the Central Government in consultation with the National Development Council.

(Para 16.4)

77. Assistance in the form of grants and loans for certain non-developmental purposes outside the plan may continue to be provided as at present by the Central Ministries. (Para 16.5)

National Development Bank

78. Central loans to States for financing identifiable projects in fields like power, transport, irrigation and manufacture, should be channelled through a new institution to be known as the National Development Bank, which should be built up in a phased manner over the next few years. The contemplated arrangement would apply to both Central and State projects so long as these fall in the defined category. (Para 17.2)

79. The institution devised, besides being development-oriented, has to be professional and business-minded. While granting financial assistance, it would initiate steps for effective supervision of the projects and observe business principles in sanctioning instalments etc. (Paras 17.3 & 17.4)

80. The following three considerations have to be kept in view as regards the functioning of this Bank:

- (i) This Bank should deal with loans only.
- (ii) The States should meet the cost of the projects upto a stipulated limit.
- (iii) There might be need to introduce softer loans.

(Para 17.5)

81. While the broad sectoral as well as regional pattern of assistance would be determined by the Planning Commission, the loan financing of individual projects - whether State or Central - would be left to the discretion of the Bank and would depend on the rational appraisal of the planned projects and their actual implementation.

(Para 17.6)

82. The activities of the Bank may be extended in stages. Starting with the financing of the expansion of existing projects and projects with known techniques of production, the projects of a manufacturing type and hydro-electric and irrigation schemes etc. may be taken up in that order. Projects that would not qualify for being financed by the National Development Bank would continue as before to be financed by the Central and State Governments concerned.

(Para 17.9)

83. While in the beginning the resources of the proposed Bank have to be provided in the Central Budget, in course of time, the Bank could raise loans on its own from the market - domestic as well as abroad. (Para 17.10)

84. As regards the organisational aspects of the National Development Bank, the equity capital should be wholly subscribed to by the Government of India. The general superintendence and direction of the affairs and business of the Bank should vest in a Board of Directors, which will be guided

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by the broad policy directives given by the Government of India, and act on business principles with due regard to the interests of national development. (Para 17.11)

85. The Bank may have either a part-time or whole-time Chairman. He should be a person pre-eminent in industry, commerce, finance or banking and unconnected with Government. It should also have a Vice-Chairman. If the Vice-Chairmanship of the Bank is part-time, a Member of the Planning Commission could fill this post to ensure better coordination with the Commission. (Para 17.12)

86. The bonds of the Bank would be fully guaranteed as regards the payment of principal and interest, by the Government of India. The Bank would not however accept deposits from the public. (Para 17.13)

87. The National Development Bank should have adequate trained staff to make technical appraisal of projects as well as supervise and watch the performance of selected projects. The Bank should utilise specialised consultancy and other services to the maximum extent possible to economise on over-heads.

(Para 17.14)

Borrowings by States:

88. To avoid overdrafts, the State Governments should indicate the limits of the grants to their disbursing officers which they can spend and the controlling officers of the State Government should exercise control

over disbursements and check the progress of expenditure against the grants allotted, in consultation with the Accountant-General concerned. (Para 18.7)

89. As an effective safeguard against the overdrafts of State Governments, a suitable provision may be made in the Reserve Bank of India Act that the borrowings of State Governments from the Bank should not go beyond a certain proportion of their current revenues. (Para 18.8)

90. The above restriction should apply mutatis mutandis to the Central Government also in respect of its own borrowings from the Reserve Bank. (Para 18.9)

91. As an alternative, State Governments may be required to borrow from the State Bank of India and its subsidiaries. As a corollary the balances of the State Governments would have to be transferred to these Banks. (Para 18.10)

92. It would be a good idea if the public borrowing programme of all the State Governments was centralised. Though not conspicuously successful in the past, it should be given a further and more systematic trial. There should be greater coordination between the Central Government and the Reserve Bank in the matter of State borrowings. (Para 18.13)

93. The small savings programme as operated at present has not succeeded in its principal aim of fostering new savings and the cost of operating the schemes in respect of low-income groups is relatively high. The scheme of post office

savings deposits has been successful and this part of the programme should be encouraged through suitable measures. (Para 18.14)

New Delhi,
May 27, 1967.

Sd/-
(P.Venkatappiah)
Chairman

Sd/-
(N.N.Wanchoo)
Member



Sd/-
(P.L.Tandon)
Member

Sd/-
(G.L.Pansal)
Member

Sd/-
(N.S.Pandey)
Member

Sd/-
(J.C. Luther)
Secretary, Study Team

Sd/-
(D.T.Lakdawala)
Member

A P P E N D I C E S



सत्यमेव जयते

APPENDIX I

Memorandum relating to the Constitution of the Study Team on Financial Administration.

Appendix I(i) -- Memorandum of the Administrative
Reforms Commission dated May 28, 1966.

The Administrative Reforms Commission hereby appoints the following persons to constitute the Study Team on Budgetary Reform, System of Expenditure Control and Procedure governing financial relations between the Centre and the States:

- | | |
|---|----------|
| 1. Shri B. Venkatappiah,
Mafatlal House,
Backbay Reclamation,
Bombay-1. | Chairman |
| 2. Shri N.N. Wanchoo,
Secretary,
Ministry of Iron & Steel,
New Delhi. | Member |
| 3. Shri P.L. Tandon,
Chairman;
Hindustan Levers;
165-166 Backbay Reclamation,
Bombay. | " |
| 4. Shri G.L. Bansal,
Secretary-General,
Federation of Indian Chambers
of Commerce & Industry, Federation House
New Delhi. | " |

2. The Study Team will, in regard to the subject allocated to it, ascertain facts, locate the principal problem areas, examine solutions for the problems and suggest such of them as they would recommend for the Commission's consideration. The Study Team will submit its report as early as possible.

3. Shri J.C. Luther, Deputy Secretary, Administrative Reforms Commission, will act as the Secretary of the Study Team.

Appendix I(ii) -- Memorandum of the Administrative
Reforms Commission dated June 20, 1966.

The Administrative Reforms Commission appoints the following as the Member of the Study Team on Budgetary Reforms, System of Expenditure Control and Procedure governing financial relations between the Centre and the States, in addition to those already appointed vide Commission's memorandum dated 28th May, 1966:

Shri N.S. Pandey,
Joint Secretary,
Administrative Reforms Commission,
Travancore House, Curzon Road,
New Delhi.

Appendix I(iii) -- Memorandum of the Administrative
Reforms Commission dated October 1, 1966.

The Administrative Reforms Commission appoints the following as the Member of the Study Team on Budgetary Reform, System of Expenditure Control and Procedure governing financial relations between the Centre and the States, in addition to those already appointed vide Commission's memoranda dated 28th May, 1966 and 20th June, 1966:

Dr. D.T. Lakdawala,
Head of the Department of Economics,
Bombay University,
Bombay.

Appendix II

SOME IMPORTANT ISSUES REGARDING BUDGETARY REFORMS , FINANCIAL CONTROL AND CENTRE STATE RELATIONS

I. OBJECTIVES:

Emphasis on 1. The following are amongst the main objectives and functions of the budgets of modern Governments:

Accountability (a) to set out clearly a statement of receipts and expenditures, specifying the amounts voted by the Legislature, the objects on which the amounts are to be spent and the operating agencies responsible for incurring expenditure ;

Plan correlation (b) to indicate the correlation between the Development Plan as a long-term programme and the Budget as an Annual Statement ;

Functions (c) to indicate to the extent possible, the functions - administrative, social, developmental and other - which are sought to be subserved by the funds voted by the legislature and the costs of such functions ;

Programmes (d) to outline the programmes and activities proposed to be undertaken by Government together with the cost involved in them. ;

Performance

(e) to set out in terms of physical targets (wherever possible) the programmes sought to be executed by Government together with an indication of past performance;

Management

(f) to serve as an aid to better management in the planning, execution, control and review of programmes;

Economic
significance

(g) to indicate the economic significance of the programmes and policies envisaged in the budget; and

Government
policy

(h) to serve as an instrument of Government policy.

These functions and objectives are not mutually exclusive; in fact, the budgets of many countries are so designed as to serve multiple objectives, with a difference only of emphasis.

Which of the objectives mentioned above would you consider specially important to Government budgeting? Are there any other objectives which in your opinion are important?

2. Do the budgets of the Central and State Governments fulfil the desired objectives? If not, what modifications would you suggest?

II FORMULATION OF THE BUDGET:

3. The Financial Year

It has often been suggested that the present financial year extending from the 1st of April to the 31st of March is unsuitable for various reasons such as uncertainty at the time of budget preparation about the south-west monsoon which has a dominant influence on our economy, the loss of a part of the working season in the beginning of the year due to the non-availability of sanctions of funds and the inability of the members of the Legislature to tour their constituencies at a convenient time. The 1957-58 Estimates Committee (20th Report, Second Lok Sabha) had suggested that the financial year may be changed to commence from the 1st of October. There have also been suggestions that the financial year should commence on the 1st of January or the 1st of July. What are your views on this point?

4. Contents of Budget Papers:

The following are the main documents which are presented to Parliament in connection with the Central Budget.

- (1) the main Budget consisting of a General

Statement of Revenue and Expenditure met from Revenue and a General Statement of Receipts and Disbursements, together with Detailed statements of revenue, and expenditure met from Revenue, and Detailed Statement of Receipts and Disbursements.

- (ii) Explanatory Memorandum
- (iii) Demands for Grants
- (iv) Economic Survey
- (v) Annual reports of Ministries
- (vi) Annual Report on the Working of Industrial and Commercial Undertakings of the Central Government.
- (vii) An Economic Classification of the Central Government Budget.

Although the form and contents of these documents have been reviewed and revised from time to time in order to provide more useful and meaningful data, it has often been represented that these documents still do not give comprehensive information which would be of interest to the members of the Legislature and the common citizen. Some of the points made in this connection are:

- (a) the entire cost of a service or a function is not given in

any one place in the Demands for Grants;

- (b) the Explanatory Memorandum does not give full information about the actual utilisation of loans and grant-in-aid given by the Centre to the States;
- (c) the Annual Reports of Ministries do not contain a sufficiently informative review of important schemes with reference to targets and achievements in physical and financial terms.

What, in your opinion, are the areas in which sufficient information is not available in the budget? Please indicate your proposals for overcoming these deficiencies in the light of the problems and difficulties which may arise in implementing them.

5. Preparation and Scrutiny of Budget Proposals:

There has been a continuing criticism of lack of accuracy in Government Budgets. It has been pointed out that the estimates of revenue are not based on any systematic

analysis and there is a persistent tendency to under-estimate revenue receipts. On the other hand, the estimates of expenditure are often found to be on the high side on account, partly, of indifferent planning and scrutiny of new schemes and unsatisfactory appraisal of continuing schemes. Another reason for loose budgeting is stated to be the considerable delay in the availability of information on the progress of expenditure with the result that in October/November, at the time of framing the Revised Estimates in the current year and the Budget Estimates for the ensuing year, accurate information in respect of the progress of expenditure is available only till the month of July. It has been pointed out that lack of proper budgeting leads to such undesirable features as the provision of lump-sum and token grants, large savings and lapses of grants and the rush of expenditure towards the end of the year.

Please indicate what, in your opinion, are the basic reasons for such shortcomings in the budget as the under-estimation of revenue, the over estimation of expenditure and inclusion in the budget of immature schemes or schemes without any details.

What are your views on the adequacy of the present arrangements for the preparation and scrutiny of budget proposals at various stages e.g. in the Administrative Ministry, the different wings of the Ministry of Finance, and the Planning Commission. If you consider the present arrangements inadequate, what remedies would you suggest?

6. The Budget and the Plan:

The lack of correlation between the annual plan and the budget both in the Central Government and the State Governments has been commented upon as a serious weakness of the present system, It has been pointed out, for example, that the developmental heads adopted/for budgetary and accounting purposes with the result that it is difficult to identify in full the expenditure included in the budget in respect of the various plan schemes.

in the plan are at variance with the major heads adopted

What are your suggestions for achieving a better integration between the Budget and the Plan so as, among other things, to facilitate evaluation of the progress of Plan schemes simultaneously with a review of the Budget.

Please set out your views in detail indicating the practical lines on which your suggestions can be implemented.

7. Department-wise grants:

The budget estimates are prepared on a departmental basis. The governing factor for classification is not the nature and objectives of the receipt and expenditure but the department or agency which has to collect the receipts or to incur the expenditure. For instance, the provision for the building of a school or hospital is included in the P.W.D. Grants and not in those of the Education Ministry or Health Ministry.

What are your views on the merits of the present system? Would you advocate any change in this regard?

8. Programme Budgeting:

It is said that the dominant feature of the Indian Budgetary system is its emphasis on accountability: the system is not designed to suit the formulation and execution of specific programmes with emphasis on identification and achievement of specific targets in measurable terms. It has been suggested that the concept of programme budgeting should be employed

to recast or supplement the present budget.

Do you consider having regard to the institutional set-up and other relevant factors, it is necessary and feasible to introduce programme-cum-performance budgeting in India? If so, what practical steps and stages would you recommend for implementing this suggestion?

9. Classification:

It has been said that the present system of classification of revenue and capital transactions is largely governed by administrative considerations unrelated to any scientific principles. For instance, there is a monetary limit for expenditure on new works which can be met from Revenues.

It has also been observed that while the demands for grants give separately the expenditure on Plan schemes, they do not exhibit non-Plan Developmental Expenditure. Further instances of this type could be mentioned.

Do you have any comments to make on these or other aspects of classification adopted in the Indian Budget?

10. The Budget in Parliament:

There is a general feeling that the limitations of time and procedures in the present system do not give Parliament sufficient opportunity to examine and discuss budgetary plans and schemes in detail. It has been suggested in this connection that:-

(a) the Standing Finance Committee which used to exist before the inauguration of the Constitution in 1950 may be revived to provide an opportunity to the members of Parliament to scrutinize new items of expenditure above a certain limit;-

(b) more time may be allotted for the consideration of each Ministry's demands for grants;

(c) the demands may be discussed by the whole House sitting as the Committee of Supply as in the U.K. in an informal manner uninhibited by formal rules and procedures;

(d) the House may divide itself into a few smaller committees for detailed examination of the grants for various Ministries.

What are your views in this connection?
Have you any suggestion to make?

III

EXECUTION OF THE BUDGET:

11. Delay in issue of sanctions:

It is said that valuable time in the months of April and May is lost in the execution of budgetary programmes in the new year on account of delays in the issue of sanction for schemes to be implemented by the Central Government as well as the Centrally sponsored and Centrally-assisted schemes to be implemented by the States.

The continuity in the progress of current schemes is also said to be affected by break in the flow of sanctions as a result of the timelag before the issue of sanctions in the new year.

Do you agree with these observations?
Kindly give your comments with particular reference to the adequacy or otherwise of the present system of Vote on Account which is intended to temporarily provide funds for all schemes with the exception only of New Services to which such amounts cannot be applied. If the slackening of progress in the early months of the new year cannot be attributed to budgetary

constraints, what do you think are the other administrative or procedural deficiencies which are responsible for this state of affairs? Do you think the Rule of Lapse of Funds at the end of the year has a bearing on this problem? In this connection various remedies have been suggested. It has been proposed by some that the annual grants should not lapse by the 31st March, but that they should be allowed to be carried forward for a few months, say, till the end of June; another suggestion is that the grants should be sanctioned for a longer period, say, two years and that in some cases non-lapsing grants should also be sanctioned. What are your comments on these points?

12. Objectives of Budget Execution:

It has often been said that adequate arrangements do not at present exist for the follow-up and review of budgetary programmes. Adequate attention is not paid to regular and careful reviews of the progress of expenditure in financial terms in relation to the available appropriations. As for the physical targets envisaged in the various programmes, the review or appraisal is even less satisfactory.

If you consider the present procedures unsatisfactory, what suggestions for reforms would you offer?

13. Delegation of financial powers:

An important feature of the recent financial reform in the Government of India is the delegation of enhanced financial powers from the Ministry of Finance to the Administrative Ministries and from the Administrative Ministries to the operating Agencies subordinate to them. At present, the relations between the Finance Ministry and the administrative Ministries in this regard are governed by the scheme introduced in June, 1962 and further clarified in the Finance Ministry's O.M.No.F.10(50)-E(Coord)/65, dated the 15th March, 1966. Accordingly, the financial powers of the Ministries have been considerably enhanced in respect of staff recruitment, appropriation and re-appropriation among primary - units, and contracts and projects, etc. Also the Ministries now have full powers subject to funds being available, to sanction expenditure on schemes, irrespective of the magnitude of such expenditure, provided the projects as a whole have been previously scrutinised and accepted by the Ministry of Finance.

It is held by some that the enhanced powers are available to Administrative Ministries only in name and not in practice and that the control of the Ministry of Finance has not been much relaxed. It has been pointed out in this connection that the Ministry of Finance take too much time in approving the projects as a whole with the result that piece-meal references are still required to be made to them on several schemes even in the Post-Budget period. On the other hand, the Administrative Ministries are said to have shown little willingness to exercise all the powers delegated to them and even cases in which they are competent to decide continue to be referred to the Finance for 'advice' and/or 'concurrence'.

Would you consider that the powers delegated to the Administrative Ministries and by them to the authorities subordinate to them are adequate? If not, what modifications would you suggest? Please give your suggestion also on improvements in the policy and procedures with a view making delegation more effective.

14. Scrutiny by Finance:

An essential feature of the present ^{the} relations between Ministry of Finance and the Administrative Ministries is that the control by the Finance Ministry will be mainly through pre-budget scrutiny and through random checks, and work studies. However, the budget still provides for schemes on lump-sum or token basis either because the Ministries are unable to prepare necessary details on certain urgent schemes or such details as have been furnished by them have been adjudged in-adequate by the Finance Ministry. The result is that a number of schemes continue to be referred to Finance, for post-budget scrutiny although the schemes are included in the Budget. It has been suggested that this practice is responsible for considerable delay in the implementation of schemes.

If you share this view, would you give your comments on the underlying reasons and possible remedies for this situations (i) in the Central Government, (ii) in the State Government.

15. The Role of Financial Adviser:

It has been suggested that there should be integration of administrative responsibility and financial control in the operating agencies and Administrative Ministries. Under the present arrangements in the Government of India, it has been left to each Administrative Ministry to decide whether a Financial Adviser within the Ministry is required for it or not. It is also envisaged that the Finance, Budget and Accounts work within the Administrative Ministry will be organised on a scientific basis under the control of the Internal Financial Adviser, where one exists, or a senior officer specially nominated for the purpose.

Please indicate, in some detail your views on the role of the Financial Adviser with special reference to the following points:

- (1) Should the Administrative Ministry have a Financial Adviser under its own control or should he be under the control of the Ministry of Finance? .

(ii) In either case should the Secretary of the Administrative Ministry have the power to over-rule the Financial Adviser? Do you consider it desirable to lay-down specific procedures to regulate the relations between the Secretary and the Financial Adviser?

(iii) What should be the relation between the Internal Financial Adviser and the Ministry of Finance.

(iv) Should the Secretary of a Ministry himself act as the Chief Accounting Officer? In other words, should the payment and Accounts organisation be placed directly under the charge of the Secretary as at present? If so, what should be the role of the Financial Adviser in regard to such matters as control of appropriations and pre-audit checks on expenditure.

16. Expertise in Financial Control:

It has often been pointed out that the recent reforms in the system of expenditure control have been mainly directed towards the regulation and

adjustment of inter-relations between the Ministry of Finance and the Administrative Ministries; not much attention has been given to the need to develop and maintain specialised talent, well equipped in modern skills and techniques of budgetary and other financial controls. With the extension of Government activities into complex spheres of economic and industrial activities, the need has been felt for specialised personnel and techniques to render financial advice. It has been pointed out in this connection that the lack of expertise in principles and methods of financial control in the Administrative Ministries has resulted in poor planning and performance on their part and consequently in delays and difficulties in securing the approval of Finance to their schemes. It has sometimes been suggested that interchangeability of officers between the Finance and other Ministries would go a long way in developing financial skills and in promoting efficiency in the exercise of financial control.

What are your views in this matter?
Please give your complete suggestions for improving the methods of budgetary and

expenditure control, both in the Administrative Ministries and in the Finance Ministry.

Would you advocate the creation of a specialised pool of officers with financial background and training?

17. Control over Public Sector Undertakings:

It has sometimes been urged that there is too much interference from the Government in the management of Public Undertakings and that this has an adverse effect on their initiative and efficiency. There is also the opposite point of view that the Public Sector Undertakings have been given too much freedom and the arrangements for their control and supervision by the Government are not adequate.

What are your views in this regard?
Please illustrate your comments with reference to specific features of the present pattern of relations between the Government and the Public Undertakings.

18. Budget of Public Undertakings:

It has been suggested that the pattern of financial control over ^{the} federal corporations in the U.S.A., as laid down in the Government Corporation Control Act, of 1945 should be followed in India also and business-type

budgets including data on programmes and performance should be prepared by them for review and approval by Government. Would you favour this type of centralised control in some or all Public Undertakings?

IV REVIEW:

19. The Estimates Committee of Parliament is concerned with the examination of the Estimates from the view point of ensuring economy in governmental expenditure consistent with the declared policy. The Public Accounts Committee scrutinise the Appropriation Accounts and the reports of the Comptroller and Auditor General on the Accounts with a view to ensuring, inter alia, that the expenditure conforms to the authority which governs it.

(1) It has been suggested that the functions of the two Committees overlap in important areas and a more complete and unified system of Parliamentary review would be desirable. It is urged that the Committees should be merged into one committee which should be able to cover the whole range of estimates more adequately.

What are your views in this regard?

(ii) It has been observed that the present budgetary data does not give any evaluation at all of ^{the} past performance. Even when the actual expenditure is given in respect of the preceding year, the relevant data of estimates are not given so that it is not possible to know how far the Government has been able to perform in accordance with the Budget Estimates.

Do you consider it necessary to introduce any change in this regard?

(iii) The time lag between the closing of the financial year and the compilation of the Appropriation Accounts and the Audit Report relating to that year is rather long.

Do you have any suggestion to reduce the time-lag?

FINANCIAL RELATIONS BETWEEN THE CENTRE
AND THE STATES:

20. Co-ordination of Financial Relations:

In recent years the States' responsibilities have grown far out of proportion to their revenues. The gap between the States' own resources and the needs of their expanding functions has been widening

progressively with the implementation of development plans. This has necessitated a phenomenal growth in the size of Central loans and grants to the States outside the purview of the Finance Commission. The procedures governing financial relations between the Centre and the States have been getting more and more complicated due to the multiplicity of channels of financial assistance and the complex procedures connected with them. It has also been remarked that there is a growing tendency to overlap in the functions of the Finance and Planning Commissions.

The recent increase in the ways and means advance of the States from the Reserve Bank has been another satisfactory feature.

A suggestion has sometimes been made that the present system of a quinquennial review by an ad hoc Finance Commission should be replaced by a systematic and continuous review by a permanent body such as the Australian Grants Commission.

It is claimed that such a device would also serve to co-ordinate the

various resources of assistance, ensure an optimum mobilisation of the States' resources and enforcement of better budgetary and financial discipline.

What are your views in this matter?

Do you have any other suggestions for reforms in the procedures governing the financial relations between the Centre and the States?

21. Central loans to the States:

The practice of granting loans from the Centre to the States is somewhat unusual as in other federations, such as the U.S.A., Canada and Australia, the Central Government makes only grants to the federating units. In India complex problems have arisen as a result of the phenomenal growth in the size of Central loans, their vast number and immense variety as regard different rates of interest and periods of repayment. The strain on the resources of the States in servicing and repayment of loans has also created difficulties. It has, sometimes, been suggested that the existing complex of loans should be simplified by a process of consolidation. It has also been suggested that a way would be found to ensure that the loans are repaid by the States only

out of their revenue surpluses.

What are your views in this regard?

Please indicate any other suggestion which you may have on this subject.

22. Release of Funds:

It has been stated that the procedures for release of funds by the Centre are cumbersome and dilatory. Although the procedures have been streamlined from time to time, the situation is still not considered fully satisfactory.

It has been pointed out, for instance, that there is an unnecessary multiplicity of patterns of financial assistance.

The limitations on the States' discretion to divert funds from one scheme to the other have also been criticised in this connection.

What are your comments and suggestions in this regard?

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Appendix III

DETAILS OF MEETINGS WITH THE CENTRAL AND STATE GOVERNMENT OFFICERS.

<u>Participants</u>	<u>Dates of meetings</u>
(i) Officers of the Central Government	27th, 28th and 29th December, 1966, at New Delhi.
(ii) Officers of the State Governments of Maharashtra, Gujarat and Madhya Pradesh.	5th, 6th and 7th January, 1967, at Bombay.
(iii) - Officers of the State Governments of Uttar Pradesh and Rajasthan.	10th and 11th January, 1967, at New Delhi.
(iv) Officers of the State Governments of Madras, Mysore, Andhra Pradesh and Kerala.	19th, 20th and 21st January, 1967, at Madras.
(v) Officers of State Governments of West Bengal, Assam, Bihar and Orissa	31st January and 1st February, 1967, at Calcutta.
(vi) Economic Secretaries to the Government of India.	4th May, 1967 at New Delhi.

Appendix IV 11)

ADMINISTRATIVE REFORMS COMMISSION

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THE EXTRACTS FROM THE MINUTES OF
THE MEETING OF 2ND AND 3RD AUGUST
REGARDING THE SETTING UP OF THE
WORKING GROUP ON PERFORMANCE
BUDGETING AT NEW DELHI

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2. The proposal in Shri N.S.Pandey's note on Performance Budgeting for setting up a small Working Group to examine in detail the various aspects of the concept underlying the techniques of Performance Budgeting and its applicability to Indian conditions was approved. It was decided that this Working Group should comprise:

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|---------------------------------------|--|
| 1) Shri N.S. Pandey, (Convener) | Administrative Reforms Commission. |
| ii) Shri J.C. Luther | -do- |
| iii) Shri A.R. Shirali or his nominee | Ministry of Finance, (Budget Division) |
| iv) Shri E.R.K. Menon | Planning Commission (Development Admn. Unit) |
| v) Shri S.S. Viswanathan | -do- |
| vi) Shri A. Prem Chand | -do- |
| vii) Dr. M.J.K. Thavaraj | Indian Institute of Public Administration. |

The following would be the terms of reference.

- i) to analyse and enunciate the principles underlying performance budgeting;
- ii) to examine the applicability of these principles to Government budgeting in India, and, in this connection, to make an attempt to recast and reclassify, on the lines of a performance budget, the operations of a few selected organisations out of the Ministries of the Central Government and Public Enterprises; and
- iii) to report on what practical steps and measures would need to be taken if performance budgeting were to be introduced in India and to make suggestions for meeting the difficulties, if any.

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Appendix IV (ii)

Order dated the 28th September, 1966
by the Chairman, Study Team on
Financial Administration.

In pursuance of a proposal discussed at a meeting of the Study Team held early in August, I have contacted various persons from the University of Bombay, Reserve Bank of India and the Government of Maharashtra in connection with the setting up of a Working Group for studying problems connected with "State finances and Centre-State financial relationship". As a result, a Working Group has been set up and met informally today in my room. It will have its first session on Saturday the 1st of October and will try to submit its report by the middle of November, 1966. The composition and terms of reference of the Working Group are as follows:

Composition

- | | |
|---|----------|
| (1) Dr.D.T.Lakdawala,
University of Bombay | Chairman |
| (2) Shri K. Ramakrishna Ayyar,
Financial Adviser to
Maharashtra Government. | |
| (3) Shri S.G. Tungare,
Deputy Secretary,
Finance Department,
Maharashtra Government. | |
| (4) Shri J.C.Luther,
Deputy Secretary,
Administrative Reforms
Commission. | |

* (5) Shri M. Narasimham,
Deputy Economic Adviser,
Reserve Bank of India.

(6) Dr. V.V. Bhatt,
Director of Planning &
Special Studies,
Reserve Bank of India.

(7) Dr. D.R. Khatkhate, Convener
Director,
Unit of State Finances,
Reserve Bank of India.

* Later replaced by Shri S.D. Deshmukh,
of the Unit Trust of India.

Terms of Reference:

(i) With reference to the States, to
examine and suggest improvements, both
generally and with particular reference to
development schemes in the Plan and outside
it, in -

(a) the methods and procedures relating
to the formulation, presentation,
approval and execution of the Budget;

(b) the systems of expenditure control
with particular reference to the
role of the Finance Departments of
State Governments.

(ii) To examine and suggest improvements
in procedures for determining the quantum of
Central assistance and the procedures involved in
the release of such assistance by Union Government.

(iii) To examine and suggest improvements in the present procedures relating to centrally sponsored and centrally assisted schemes in the State sector with particular reference to their co-ordination with the State Plans.

(iv) To examine and suggest improvements in the present procedures with regard to the borrowings by the States from the public, from the Centre or the Reserve Bank of India.



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